It’s time to talk about scale

How to get more social enterprises to scale and why we need to

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About Big Society Capital

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Working with expert partners, we seek to understand people's needs first. Then, using our knowledge and capital, we collaborate and invest with fund managers who also want to create a better, sustainable future.

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We want to give more people and communities the chance to have an impact on the issues they care about – from affordable homes to vulnerable older people, and preventing mental ill health.

We have a vision where every investment helps improve people's lives, and where others can achieve an impact way beyond our investment.

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Table of Contents

Executive Summary

Capitalism has lifted many people out of poverty[1], but now needs rethinking to achieve more. I believe the most pragmatic way to achieve a fairer, more inclusive and more equitable society is by using existing structures in better ways. In essence, making markets work for everyone.

Social enterprises have a critical role to play in delivering this ambition. They do this by intentionally creating positive change to people's lives and the planet (impact) through their business models in a range of ways. Although not all social enterprise business models deliver impact through earning income (versus those who donate surplus profits or employ vulnerable people), for many, scaling up the size of their organisations could result in substantial growth in their impact.

Scale is a choice. It is not and should not be the goal for every social enterprise. In its 2015 article, "What's Your Endgame?" the Stanford Social Innovation Review identified six 'End Games' for non-profits to ensure impact at scale: Open Source, Replication, Government Adoption, Commercial Adoption, Mission Achievement, and Sustained Service[2]. Scaling an organisation's size is only explicitly mentioned in one of these six: Sustained Service. However, some other end games may not happen without a certain level of organisational scale, such as adoption by government or corporates. I believe that if organisational scale is achieved in the cases that merit it, while ensuring impact fidelity at scale, this would be a good thing.

I started my career in the UK social sector in 2010 as an On Purpose Associate placed at HCT Group, one of the UK's most influential and well-known social enterprises. At that time, it was turning over around £20 million. It now has turnover greater than £60 million, and is going from strength to strength. When I ask people to name their favourite large social enterprises, HCT inevitably comes up alongside three or four others.

Why is it that people struggle to name more scaled social enterprises? Is it because there aren't many to name? Is it because we don't 'count' very large trading charities, like Turning Point, as social enterprises? It actually could be caused by a few things: their relative small number and scale as compared to the commercial sector, inconsistent definitions as to what constitutes a social enterprise, B2B or B2G social enterprises with lower brand awareness (i.e. Housing Associations and NHS spinouts), and a lack of awareness of social enterprise as a movement in general.

Social enterprises contribute 3% of the UK's GDP – what might the UK look like if they had more market share? If we believe it would be a substantially better place, unified efforts should be made to support more social enterprises to scale up successfully. This report takes an in depth look at what is needed to get more social enterprises to scale, comparing them to their commercial counterparts and making recommendations to create the best conditions for success.

Definitions

This paper looks at how to support existing social enterprises to scale, rather than start-ups – a different challenge altogether. The UK, in fact, has a vibrant start-up ecosystem but ranks 13th in the OECD for scaleups[3]. It is evident that the UK needs to provide more support to its scaleups, and ensure that a fair proportion of that support is designed specifically for ones intentionally delivering social outcomes.

Starting with definitions, this report uses the Social Enterprise UK definition of a social enterprise.

> A social enterprise has the following common characteristics:
> - An enshrined primary social or environmental mission, through legal form, governing documents or ownership for instance;

[1] Between 1990 and 2010, the number [of people in extreme poverty] fell by half as a share of the total population in developing countries, from 43% to 21%—a reduction of almost 1 billion people. https://www.economist.com/leaders/2013/06/01/towards-the-end-of-poverty

[2] https://ssir.org/articles/entry/whats_your_endgame

[3] ScaleUp Institute: Annual Scaleup Review 2018, p5

> Principally direct surpluses towards that mission;
> Independent of government;
> Primarily earns income through trading, selling goods or services; and
> *Has a commitment to strong Environmental, Social and Governance performance*

This paper adds a requirement for those businesses to have proper Environmental, Social and Governance (ESG) policies, practices and procedures in place. As businesses intending to generate positive impact, they should be setting an example of holistic approaches to improving people's lives and the planet throughout their operations and governance.

Social enterprises deliver impact through their business and operating models. This can be achieved using the following impact models, with many social enterprises employing more than one:

1. **Value proposition.** The product or service itself intentionally addresses a social or environmental challenge, often in line with one or more of the Sustainable Development Goals (SDGs) (e.g. education and care providers, housing associations, Polipop, HCT Group, social impact investing fund managers)
2. **Impact through Customers.** The product or service is designed for, affordable and accessible to, and purchased by low-income, vulnerable or disadvantaged customers, or with those groups identified as key target customers among other segments (e.g. Unforgettable, Fair For You, Base-of-Pyramid models)
3. **Impact through Employment.** A proportion of staff are vulnerable or disadvantaged people, with fair working conditions and benefits (e.g. Auticon, Goodwill Solutions, Social Bite, HCT Group)
4. **Impact through Supply Chain.** Ensuring fair pricing and safe working environments for social enterprise suppliers or vulnerable direct producers, or repurposing or diverting waste (e.g. Fair Trade, Café Direct, Rubies in the Rubble, Elvis & Kresse)
5. **Impact through Profits.** Surplus profit is reinvested into solving social challenges. This includes cross-subsidy models where profitable activities pay for unprofitable ones – 92% of social enterprises use the majority of their profit to further their social or environmental goals (e.g. Buy-one-give-one model like Toms Shoes or Stand4Socks, Equity for Good - Toast Ale). In addition, 12% gift profits to a separate cause (e.g. Belu Water) while 12% are the trading arm of a charity, returning profits to parent organisations (e.g. HCT Group).[4]

By scale, this paper refers to those social enterprises with greater than £10m annual turnover or more than 50 employees. And by being ready to scale, we mean businesses with at least £1m turnover, and annual turnover or employment growth of greater than 20% sustained for three years, indicating an ambition to scale and exposure to the stresses of building a high-growth business.

Findings

Even for commercial companies, scaling is really difficult and needs specific skills and incredible focus to achieve.

> "Let's look at the data, only 0.4% of all companies reach $10 million in sales and but only 0.04% sell more than $100 million. So most start-ups fail and of those that do get past the initial stage, most fail to scale. It's climbing Mount Everest, winning the lottery, playing up front for Manchester United kinda numbers. Peter Drucker´s chilling words from his book "Innovation & Entrepreneurship" are as true today as when he first wrote it. "Entrepreneurship is risky mainly because so few of the so-called entrepreneurs know what they are doing.""[5]
>
> Professor Haslam, Director of Owners Scaleup Program at IE Business School, Madrid.

[4] SEUK State of Social Enterprise Survey 2017

[5] https://intertradeireland.com/insights/blog/is-scaling-up-harder-than-starting-up/

Composition

There is surprisingly little difference between how social and commercial SMEs look, other than social enterprises not expanding internationally as much. In fact, social enterprises are doing pretty well as a sector, and delivering higher profits than their commercial counterparts on average. There is a surprising amount of activity, including 123,000 mission-led businesses[6]. But there is a worrying lack of data on social scaleups. A key finding is the inadequacy of the data being collected by existing government surveys particularly on social enterprises, with small sample sizes and no data at all on high-growth social enterprises. The self-selection nature of many sector surveys may also contribute to skewed data and findings.

In the private sector, only 6% of SMEs are considered high growth businesses (defined as having at least 10 employees, three years old and achieving 20% growth in turnover or employee numbers three years in a row) alongside a raft of slower and no growth SMEs[7]. Very few use institutional investment to grow. The Longitudinal Small Business Survey tells us that equity finance was used by only 2% of SME employers, with only 45% of those getting it from an external organisation like another business or a venture capitalist. This means that only 0.9% of SME employers in the UK use venture capital. The reasons for this are numerous, including reluctance to give up control or ownership of their businesses.

One area in which social enterprises do struggle compared to commercial SMEs is obtaining finance, particularly in the amounts of between £100k - £250k, and over £1 million. We expect funds coming online in the last few years through the Access Foundation to have gone some way in addressing the first gap, however further quantitative research is needed to fully understand the nature of this finding.

The Patient Capital Review identified a gap in capital availability for commercial SMEs looking for greater than £5m of investment. This will be a barrier faced by social scaleups as well as their commercial counterparts, potentially at a lower investment threshold. The government is implementing a series of measures to address these findings: it should ensure complementary measures are designed for social businesses as well as commercial ones (e.g. adapting comparable but relevant changes to EIS and VCT tax reliefs to SITR, their social equivalent).

Given the similarities between these groups and the impressive £60 billion contribution of social enterprises to the UK economy, social enterprise policy, currently sitting within the Department for Culture, Media and Sport (DCMS), should be moved to the Department for Business, Energy & Industrial Strategy (BEIS). This would help address many of the data inconsistencies identified, and ensure social enterprises have seats at the right tables.

KEY FACTS

- Social enterprises contribute £60 billion to the UK economy, representing 3% of GDP
- Only 6% of SMEs are considered high-growth businesses
- Less than 1% of SME employers in the UK use venture capital

Barriers to Scale

There are barriers to scaling which are common to both commercial and social businesses. These need to be addressed for them to have a fighting chance at reaching scale, given how difficult it is to achieve. The most important barriers across all businesses are access to talent, building fit-for-purpose infrastructure and access to finance.

In particular, accessing talent with experience of having scaled a business previously is very important, as is maintaining their motivation and mental health. Different skills are required at different points of a business' growth cycle. Establishing high quality, formal and structured learning and development programmes to support existing employees to develop scaling skills is critical. The skills needed across the different phases of growth include[8]:

[6] https://www.bigsocietycapital.com/latest/type/blog/pursuit-impact

[7] In 2017 there were around 11,000 [high-growth] firms in the UK, accounting for around 6 per cent of the eligible population of SMEs - STATE OF SMALL BUSINESS BRITAIN REPORT 2018, Enterprise Research Centre (2018)

[8] Tom Ebbutt email, 26 August 2019

Start-up	Crafting a vision, storytelling, prototyping, sales and marketing, developing customer-facing technology, financial modelling, and capital fundraising
Growth	*All of the above, plus:* Operations, processes, replication & standardisation, operational technology, back office and enabling-function development – particularly commercial finance, people management and development, governance
Scale	*All of the above, plus:* Internal communications, capital allocation, managing through others, leadership at scale, developing people without progression as a core driver

As social enterprises grow, they face the dual challenge of growing their operations sustainably and making a financial profit, while simultaneously maintaining and improving the quality and quantity of impact they are delivering. As well as the scaling challenges a commercial business would face, social enterprises may also face a combination of ten additional barriers specific to them:

> Limited market sizes

> Increased operational cost and complexity due to impact models

> A lesser ability to attract and develop top talent due to low sector pay, inability to offer equity compensation, and poor talent development

> Perception of low quality coupled with less focus on branding and marketing

> Competition policy issues (i.e. State Aid)

> Lack of access to risk capital, such as equity, grant or concessionary finance

> Inconsistent service levels and being slow-to-move due to dependency on volunteers or community engagement

> Sector-specific skills gaps, like systems thinking and impact measurement and management

> Lack of incentive or motivation to scale (i.e. large sums of money are the prize for scaling commercial businesses – is the impact prize worth it without the same monetary incentive?)

> Heropreneurship (i.e. idolising those who start new ventures rather than focusing on growing what already exists) [9]

Certified B Corporations are businesses that balance purpose and profit. In the US, they are legally required to consider the impact of their decisions on their workers, customers, suppliers, community, and the environment. Many successful B-Corps are B2C brands who serve the general population, appearing on supermarket shelves and retail shop racks, giving them a wide appeal, large market presence and unique ability to grow while still delivering impact at scale. They have expanded their market sizes by employing 'value proposition' impact models that allow them to serve mainstream customers.

There are three additional barriers specific to scaling the *quality,* or fidelity, of impact while simultaneously growing organisational size.

1. **Ineffective impact measurement, data collection and learning.** The ability to measure impact, learn how it is created so as to be able to replicate it, and implement changes to improve performance is critical to scaling the quality of impact alongside business growth.
2. **Dependency on individuals with unique expertise.** If impact creation is dependent on individuals – founders or key employees – with skills, experience, a certain manner or personality and knowledge that is hard to teach or replace, it will be more difficult to scale the quality of impact through growth by finding or training more of these people.
3. **Interventions that are one-to-one, face-to-face and/or intensive.** To scale up social enterprises that create their impact through intensive, often face-to-face support, a lot more time, specialist skills and money will be needed to reach each additional beneficiary. Ensuring the right level of expertise of each individual staff member delivering a service is crucial and can be costly.

This final barrier in particular poses a risk: do all social scaleups need to be tech-based, and have broad rather than deeper, more life-changing impact?

[9] https://ssir.org/articles/entry/tackling_heropreneurship Daniela Papi-Thornton 2016

Not all social scaleups will face all of these barriers, but are likely to face at least a few. Some can be addressed using non-financial approaches, while others need investment. There are many existing support programmes, accelerators and incubators that support commercial SMEs to scale. There are also social-specific programmes, however they are much fewer and at a much smaller scale. "Scale readiness" is critical to addressing these barriers. Scale readiness is having the right team, systems and processes in place to be able to grow, and respond to ever growing sales opportunities. Most support providers identified it as crucial – much more so than investment readiness. **To see more successful social scaleups, scale readiness support is a vital ingredient.**

Sectors

Certain sectors should have an overrepresentation of social enterprises given the inherent public benefit of the good or service, and the attractiveness of that sector from a financial and competitive point of view. Social enterprises are well represented in some target sectors, either by number or size or both (e.g. health and housing), while other sectors should have more (e.g. environment, education, employment, retail grocery, recreation, regional finance).

Dedicated support needs to be provided to social enterprises operating in education, housing, grocery & food, regional banking and finance, green & renewable energy, recreation and health & social care as a first priority. One way to do this could be through sector alliances, with funders, customers and social enterprises all working together and sharing learning on what works, as well as providing necessary funding and contracts.

So what's the vision?

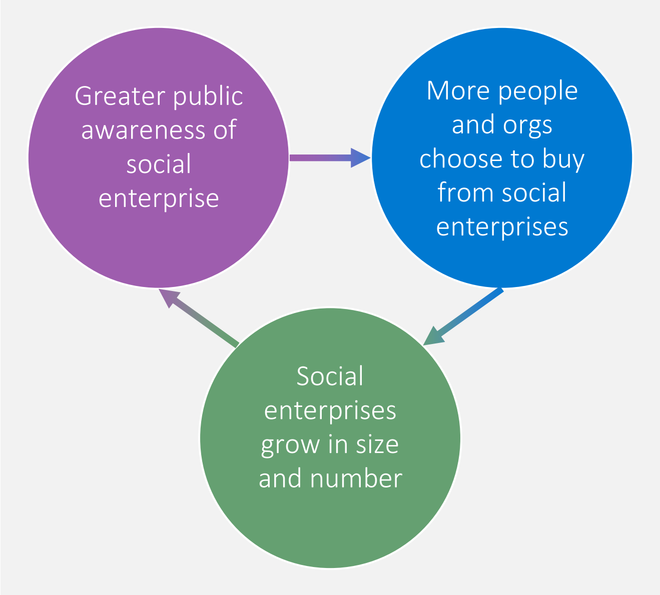
The data tells us social enterprises are doing better than we think – scaling more of them is an achievable goal. This paper puts forward a compelling and achievable vision for the future as seeing **one hundred additional social enterprises reach scale (>£10m turnover or >50 employees) across a range of priority sectors in the UK over the next five years**. This will require a shift from promoting entrepreneurship to scaling what works.

Eight areas of support are critical to see this vision through to fruition – helping social enterprises to:

1. Build, or attract, scaling skills and experience in management teams (including financial, operational and impact management)
2. Find and retain great talent through developing more effective recruitment practices and stronger talent development programmes, offering better sector wages without stigma, and seeing macro policy changes make it easier to recruit globally[10]
3. Expand to new markets, not only geographically but also reducing reliance on one or two large contracts, to a more diverse and global customer base
4. Strengthen organisation infrastructure as standard (e.g. implementing HR, CRM and finance systems, policies and procedures that can respond to drastically higher volumes of sales)
5. Ensure high quality products and services, and a skilled practice in marketing and branding, to help change market perceptions of social enterprise
6. Easily access sector-specific support to develop scalable business models, attract investors willing to pay for impact in a sector, and share resources like talent and procurement networks
7. Maintain good mental health in the entrepreneur and management team, and healthy and effective workplace cultures
8. Share and learn from successful scaling peers across sectors to help overcome challenges

A key part of the vision is to build a stronger movement around social enterprises, making it clear who they are, what they do, and how they benefit society whilst delivering high quality products and services. In this way we can create a virtuous circle of growing numbers of socially-minded businesses, all procuring from each other, and thus growing in scale themselves.

[10] ScaleUp Institute: Annual Scaleup Review 2018



Some ideas for ways to deliver the eight identified areas of support include:

> Designing a social enterprise scale-readiness programme that addresses all eight critical support areas, with a focus on barriers unique to social enterprises. This might engage a cohort of ten social enterprises per year, focused on a different priority sector each year. Depending on their needs, each would receive between £50k - £100k of grant funding per year for up to two years to allow them to purchase new systems, pay consulting fees, procure research and cover implementation costs. Assuming programme delivery costs of £200k per year[11], a total recurring annual budget for this programme would be £1.7m. **Over ten years, this programme would see one hundred social enterprises operating at scale (>£10m turnover) and creating diverse, measurable, tangible impact in the UK for a total cost of £17m.**

> Create a talent pool for candidates with proven scaling experience (addressing support areas one and two). It could identify and carefully select excellent people with track records in scaling businesses who are interested in working in social enterprises. This might also allow progression between social enterprises, enticing ambitious talent to join.

Scaleup investor BGF's Talent Network is one of the largest groups of board-level non-executives in the UK. BGF has a team dedicated to developing the Network, who match-make the most relevant non-executive directors, advisors, and experienced interim managers into the companies it backs.

> Create networks of scaling social enterprises so they can share and learn from successful peers (addresses support areas five, six, seven and eight). This could range from informal networks, to setting up new formal networks, to using existing networks like B-Corps or E3M, taking advantage of existing brands. A social enterprise scalers peer-to-peer network could be created within existing B-Corps infrastructure. This could provide leadership development opportunities, as well as a network of like-minded businesses who could procure from each other, refer others to potential clients, etc.

> In addition, local networks could be created to help scalers develop local supply chains, building and strengthening local economies. This helps create genuine impact at scale through all areas of a business' operations.

E3M is an initiative that promotes social innovation in the way public services are run. In particular, it supports the growth, scale and impact of over 30 of the UK's top social enterprises that trade in public service markets, providing them legal, financial and other expert support from partners.

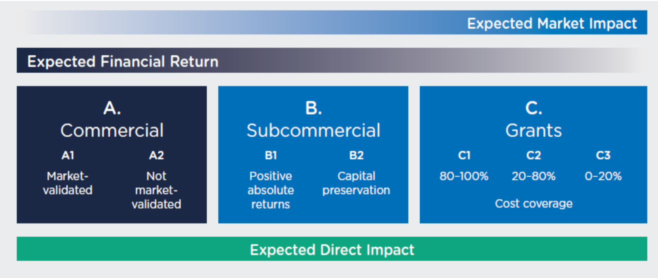
> Partner with organisations like Mind, and other ScaleUp Institute endorsed leadership programmes to provide coaching and mental health support for management team members.

Capital required to support the vision

To achieve parts of this vision, appropriate finance is required. To grow, social enterprises need capital. Risk capital allows social enterprises to take the risk of scaling up their operations ahead of being able to take on or tender for large contracts.

[11] Programme costs assumed to cover a managing director post at £90k (£110k including on costs), one programme directors at £60k (£75k including on costs), and £15k allocation for administration and office costs, assuming the programme could be hosted at a partner organisation's premises. The resulting caseload of each employee would be supporting no more than five businesses to scale per year. All consultancy and research costs would come out of each business' grant funding.

Omidyar Network has developed and made public a useful framework, the Returns Continuum, to help itself think more clearly about investing with a dual purpose of profit and impact. It identifies different segments of social enterprise, each with different characteristics, each requiring different kinds of capital:



Segment	Description of social enterprise model	Access to Finance
A1[12]	Potential to deliver market-rate return, and already has market-rate investors	Market operating properly: likely significant access to potential investors
A2	Potential to deliver market-rate return, and does NOT have equity market investors	Market-rate equity investors could invest, but have not yet due to lack of track record, and information asymmetry, mainly on the impact of the social model on the risk-return potential.
B1	Potential to deliver positive but *less* than risk-adjusted market-rate returns	Market-rate equity investors will not invest; requires catalytic capital or other intervention to access capital. Depending on model, debt-like market-rate capital may be available such as bonds and leasing.
B2	Potential to return only initial capital	Market-rate equity investors will not invest; requires catalytic capital or other intervention to access capital. Unlikely debt investors will be available.
C	No ability to return initial stake	Grant funding required

In practice, businesses will rarely fit wholly in one segment, and might move between segments at different points in their lifecycles. Nevertheless, this is a useful framework for considering financing solutions across different business models. The focus of this research was Segments A2, B1 & B2.

For businesses in Segment A2 that have the potential of delivering market-rate returns, capital can be made available to validate their models, subsequently attracting in commercial capital. Impact investors are a good fit for this segment, but will still need to be convinced their capital will have both a big impact and sizeable returns to compensate them for taking a higher risk on a not-yet-validated model. Other mechanisms that can encourage investment include guarantees, and raising catalytic capital from investors willing to take junior positions to ensure deals go ahead. Investment from institutional and professional investors gives confidence to potential investors that proper due diligence has been completed and robust decision-making has taken place.

In addition to these investment interventions, de-risking the ventures themselves will increase their chances of success, theoretically crowding in more capital. Four components together can de-risk social scaleups:

1. Strong infrastructure in terms of team, systems, sales processes, and controls
2. Shared talent pools & stronger people strategies
3. A stronger social enterprise movement
4. Market-side initiatives, such as smaller contract sizes and strengthening the Social Value Act

Finally, making capital available across longer investment time horizons is crucial. Finding investors that do not expect an exit within five to ten years will ensure more social scaleups achieve investment.

For those social enterprises in Segments B1 or B2, the picture is not quite as clear. To get investment, by definition they will need to find concessionary capital willing to accept sub-market rate returns. Concessionary capital should, in fact, play a critical role in supporting social scaleups across every segment. Four types of investors might be willing to provide this kind of capital: Government, Foundations, venture philanthropists, and individuals.

[12]Segment A1 is excluded from the analysis in this paper as capital is already available. Segment C is also excluded because of the continuing reliance on grant funding, with no apparent role for repayable finance. Models in Segment C are able to scale, but will be ever-dependent on large grants from donors.

An example of government providing concessionary capital is the British Business Bank's (BBB) Enterprise Capital Funds (ECF) programme. Through this scheme, the BBB invests into venture capital funds on terms that improve outcomes for private investors if those funds are successful. It works by giving up a portion of its pro-rata upside to private co-investors, while securing a preferred return to limit its losses. It aims to increase the supply of equity to UK growth companies and to lower the barriers to entry for fund managers looking to operate in the VC market. Since inception, more than £1.2bn has been committed (£700m by BBB) through the ECF programme (at end December 2018). The ECF programme is a significant part of the UK venture capital industry, with 28 funds facilitating finance to more than 480 SMEs (as at end September 2018).

Concessionary capital is the scarcest of all resources, and is complicated for individual businesses to access alone. Investors might only make it available to businesses addressing specific causes that align with their missions, thus blanket solutions become harder to design. One solution might be to create sector-based alliances of funders, commissioners and enterprises to define shared goals and approaches between them.

A good example of this happening at a systemic level is Fair4All Finance, a new organisation created to improve access to affordable credit by building capacity in the affordable credit sector with a combination of financial support, capability development and ecosystem development programmes. It is funded through unclaimed dormant assets in the UK, and is taking a systemic view on how to bolster the affordable credit sector as a whole, while also pumping investment into a number of ready-to-scale affordable credit providers.

Conclusions

Social enterprises have the potential to change the world. They are already some of the way there, but need more support to realise their true potential. It is feasible to imagine scaling up one hundred more social enterprises in the next five years with a lot of collaboration, imagination and patience.

Recommendations Summary

Government

1. Ensure all SME support programmes are accessible to social enterprises, and designed with them in mind – particularly initiatives borne out of the Patient Capital Review.
2. Move social enterprise policy into BEIS from DCMS. This will help ensure data collection on this segment is more rigorous and aligned to existing SME policy:
    - Align research on High-Growth Social Enterprises to match what is already collected on commercial SMEs in the Government's Social Enterprise: Market Trends future reports.
    - Increase sample sizes in future Social Enterprise Market Trends reports to provide more statistically significant data.
    - Do more research to understand the nature and needs of mission-led business.
3. Increase promotion of the existing positive level of activity of social enterprises and mission-led businesses, and support their continued growth.
4. Ensure consistency in the way the Social Value Act is being adopted by making learning, sharing and doing resources widely available.
5. Help build legitimacy of investing in social enterprise by enabling investing in social funds. This could be done by earmarking a portion of the British Business Bank's Patient Capital money for social enterprise-focused VCs and funds; or making concessionary capital available to social enterprises, funded by further Dormant Assets money or the Shared Prosperity Fund.

Wholesalers of social investment (including Big Society Capital, Access Foundation, and other Institutional Investors)

6. Identify achieving more social scaleups as a strategic aim across key sectors.
7. Focus on sectors prioritised by impact potential and need, and create sector-based funding alliances.
8. Conduct quantitative research to determine the size and nature of the capital need across

segments A2, B1 and B2 to be able to better design future funding.

9. Publish research on the use of catalytic capital in the UK, highlighting where it has and has not been successful, in order to better understand and disseminate learning about how this capital can best be deployed, as well as inspire more owners of capital that could be catalytic of what's possible. This could demonstrate to asset owners the potential of investing in uncertainty.
10. Partner with catalytic capital providers to make capital available to segments A2 and B1 by blending grant and social investment. Connect them to opportunities to deploy catalytic capital by taking junior positions in funds struggling to close fundraising rounds. New financing structures may be required to enable achievement of financial risk/return objectives. This will work to crowd in much larger amounts of capital for this segment.
11. Make more capital available to segment A2, particularly with long time horizons for repayment and realisation, allowing social investors to 'back our winners properly'.
12. Consider designing specialised funds to invest in B-Corps or Community Interest Company scaleups. This could have the potential to deliver market-rate returns, with little need for concessionary capital.
13. Support platforms that make it easier for individuals to find and invest in the causes and businesses they care most about.
14. Continue being as transparent as possible and sharing data about the market, impact and due diligence on deals to encourage others to co-invest. Enable the sector to better share and use "big data".

Concessionary Capital providers (including foundations, high-net worth individuals, government and venture philanthropists)

15. Identify achieving more social scaleups as a strategic aim across key sectors.
16. Create sector-based alliances of funders, who collate best practice approaches to maximising impact, and, taking a systems-based approach, can test and pilot new initiatives. These alliances could result in targeted, sector-focused funds that provide a blend of concessionary and commercial capital to get to a viable scale quickly. The priority sectors identified in this paper would be good places to start.
17. Create a permanent £1.7m annual scale-readiness grant fund that supports ten social enterprises to scale-up with up to £200k of grant funding across two years. The programme should address all eight critical support areas, with a focus on barriers unique to social enterprises.
18. "Grant funders should increase funding amounts (to greater than $500k) to support growth and diffusion; act as long-term partners (>5 years), not just a funder; fund core costs; and take informed risks when deciding who and how much to fund - go bigger on riskier bets when they're ready to scale." [13] Consider replicating the Catalytic Capital Consortium in the UK to chase scale with scale.
19. Purposefully design blended capital programmes that reach more of the UK's social enterprises. This would help bridge mainstream capital to the needs of enterprises in segments B or C.

> Convergence is the global network for blended finance, launched in January 2016. It generates blended finance data, intelligence, and deal flow to increase private sector investment in developing countries. There is a $2.5 trillion annual funding gap to realise the Sustainable Development Goals through philanthropy and development aid sources alone. Using grant capital to blend with traditional investment, they hope to see trillions mobilised.

20. Design a guarantee scheme, modelled on the British Business Bank's Enterprise Finance Guarantee, which reduces the risk in investing in social enterprises with scaleup potential that have not yet proven their models.
21. Depending on the results of the research on capital need in recommendation eight, consider investing in an A2-specific social

[13] https://ssir.org/articles/entry/why_proven_solutions_struggle_to_scale_up#

scaleup fund, catalysing it and attracting in commercial investors.

22. Concessionary capital can be used to support large social enterprises wanting to bid for stretch contracts and tenders by providing pre-bid scale readiness finance and support and guarantees to support their bids.
23. Continue being as transparent as possible and sharing data about the market, impact and due diligence on deals to encourage others to co-invest.

Social Investors (including intermediaries)

24. Support businesses you back to develop structured learning and development programmes specifically to build scaling skills in existing employees. Ensure a focus on good mental health in the entrepreneurs and management teams you back, and healthy and effective workplace cultures.
25. Consider designing specialised funds to invest in B-Corps or Community Interest Company scaleups. This could have the potential to deliver market-rate returns, with little need for concessionary capital.
26. Ensure sharing and learning from successful scaling peers across sectors.
27. Partner with concessionary capital providers to make capital available to segment A2 and B1 businesses. New financing structures may be required to enable achievement of financial risk/return objectives.

Support Providers (including scaling programmes like UnLtd and Impact Hub)

28. Prioritise getting social enterprises scale-ready, over investment-ready, including helping businesses understand how best to develop scaling-specific skills in their existing talent.
29. Provide more support to social enterprises to expand internationally, and obtain amounts of finance over £1 million.

Umbrella & Infrastructure Bodies (including SEUK)

30. Coordinate sector-specific alliances between social enterprises, funders and commissioners.
31. Continue building the movement around social enterprise – particularly encouraging more collaboration including shared talent pools, shared supply chains, and encouraging and enabling procurement from within the sector.
32. Develop a shared commitment with other support organisations to build scaling skills in employees of social enterprises.
33. Consider creating a scaling talent pool specifically to help social enterprises identify candidates with proven scaling experience.
34. Highlight the scaling efforts of entrepreneurs – turn scalers into heroes.

The Issue

> "The most urgent challenge in the social sector is not innovation, but replication. No idea will drive big impact at scale unless organizations—a lot of them—replicate it."
>
> Kevin Starr and Greg Coussa, SSIR[14]

The world needs help. Humans have made incredible progress over the past century, but are facing the consequences of rapid growth at any cost.

Capitalism needs an overhaul.

Capitalism has lifted many people out of poverty[15], but now needs rethinking to achieve more. This has become evident through recent geopolitical events like climate change, the European refugee crisis, as well as through mass demonstrations like the Occupy movement and Avaaz's almost 50 million person strong global network of "clicktivists" fighting injustice and inequality. Greed is allowed to play too large a role in the systems we've built. Tax evasion has cost the UK around £70 billion in revenues overall[16]. Inequality is growing: 42 people hold as much wealth as the 3.7 billion who make up the poorest half of the world's population[17]. Poverty indicators are improving, but progress is slowing[18].

Social Enterprise provides an alternative: a more inclusive and positive form of capitalism.

Social enterprises have a mission beyond profit. They exist not only to operate profitably through trading, but also to have a positive impact for people and planet. One could argue this is how all business should be operating. A thriving ecosystem of large social enterprises competing with commercial incumbents and winning at scale would begin to redress our history of growth at any cost and provide a model of growth for the future. They would demonstrate that a different way of doing business is possible - one that values every stakeholder from the environment, to the customer, to the supplier as well as the shareholder. And that business has the potential to solve our biggest challenges.

But the social enterprise sector is not yet big enough to make a dent.

Social enterprises contribute £60 billion to the UK economy[19]. The figure is staggering, but in the context of a £2 trillion economy, it represents 3%. Imagine what might be possible if we could substantially grow this market share.

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[14] https://ssir.org/articles/entry/enough_innovation_already

[15] Between 1990 and 2010, the number [of people in extreme poverty] fell by half as a share of the total population in developing countries, from 43% to 21%—a reduction of almost 1 billion people. https://www.economist.com/leaders/2013/06/01/towards-the-end-of-poverty

[16] https://www.patrickcannon.net/insights/uk-tax-evasion-statistics/ (Accessed 21 May 2019)

[17] https://www.theguardian.com/inequality/2018/jan/22/inequality-gap-widens-as-42-people-hold-same-wealth-as-37bn-poorest (Jan 2018) AND https://www.oxfam.org/en/even-it/5-shocking-facts-about-extreme-global-inequality-and-how-even-it-davos (Nov 2018)

[18] "Fewer people are living in extreme poverty around the world, but the decline in poverty rates has slowed, raising concerns about achieving the goal of ending poverty by 2030 and pointing to the need for increased pro-poor investments... The percentage of people living in extreme poverty... [is] 10%... in 2015" https://www.worldbank.org/en/news/press-release/2018/09/19/decline-of-global-extreme-poverty-continues-but-has-slowed-world-bank (Sept 2018)

[19] https://www.socialenterprise.org.uk/the-hidden-revolution (Nov 2018)

Replicating social innovation or scaling social enterprise?

Social change does happen outside of social enterprises. Stanford defines social innovation as "the process of developing and deploying effective solutions to challenging and often systemic social and environmental issues in support of social progress." [20] For really tricky, complicated issues, one large social enterprise is unlikely to achieve the systems change needed alone: multiple actors working together is the only way to make progress.

Ultimately, the most difficult and important problems cannot be solved without involving the non-profit, public, and private sectors. Social innovation seeks to create long lasting, positive impact at scale by spreading and sharing ideals, guidelines and what works more broadly through franchises, associations, fellowships, informal groups etc.

Example: Alcoholics Anonymous - impact at scale through informal structures

Alcoholics Anonymous are an international mutual aid fellowship who adhere to a set of principles (the 12 steps) and thus have positive impact in people's lives worldwide. There is an A.A. presence in approximately 180 nations worldwide, with membership estimated at over two million through more than 118,000 A.A. groups. They are not one single organisation, nor are they financially affiliated: A.A. groups are self-supporting, relying on voluntary donations from members to cover expenses.[21]

Another example is Ashoka, the global network of social entrepreneurs. As an organisation, they are increasingly focused on scaling impact without scaling the social organisation[22]. The Globalizer programme, launched in 2009, supports social entrepreneurs to develop strategies to spread their impact by transitioning from an enterprise to an ecosystem approach.

Learning to scale innovation is of utmost importance if we have any hope of solving many of the most serious problems facing our world today. Many people believe firmly, either in the power of scaling innovation by spreading ideas, or in scaling organisations dedicated to impact. Why must we choose? Surely these approaches each have their own benefits and can complement each other, existing in parallel. A non-binary approach is required to address non-binary issues.

In fact, some organisations manage to achieve both. Patagonia is a company operating at scale with the mission to "save our home planet". Along with creating a great and sustainable brand, it sued President Trump in December 2017 for reducing the size of two national monuments[23].

The Stanford Social Innovation Review identifies six types of 'Endgame' for social enterprises[24]:

ENDGAME	CHARACTERISTICS	CORE APPROACH	FUTURE ROLE
Open source	A breakthrough idea that is easy for other organizations to adopt and integrate	Conducting research and development, and sharing knowledge	Serving as a knowledge hub for research related to a break-through idea
Replication	A breakthrough product or model that is easy for other organizations to adopt and deliver	Defining a replicable operating and impact model, demon-strating its efficacy, and sharing it with other organizations	Providing certification of franchise programs and training services, and serving as a center of excellence
Government adoption	A model with high coverage potential, along with a capac-ity for integration into public sector programs	Delivering results at a sufficient scale and level of efficiency to make a case for public sector involvement	Offering services to government agencies, and maintaining research and advocacy efforts
Commercial adoption	A product or service with profit potential that solves a market failure or reduces market risk	Demonstrating the impact and the profitability of a prod-uct or service, and reducing associated risks	Maintaining advocacy and monitoring efforts, targeting hard-to-reach market segments, and working to ensure com-mercial delivery
Mission achievement	Defined and achievable outcomes related to solving a discrete problem	Maintaining a focus on tar-geted intervention	Applying (where relevant) unique assets and capabilities to additional issue areas
Sustained service	A strong organization, with a proven ability to sustain fund-ing, that fills a market or public service gap	Creating a cost-effective model, building a strong organization, and making efficiency improvements.	Continued provision of a core service at an ever-increasing level of efficiency

Table 1: Plotting an Endgame: Six Options by Stanford Social Innovation Review

Although growing an organisation's size is only one of six options to scale up or replicate impact, through building a sustained service, other endgames may depend on an organisation reaching a certain scale first, such as adoption by government or corporates. Scaling up is not for everyone, but where it can play a role, it should.

[20] https://www.gsb.stanford.edu/faculty-research/centers-initiatives/csi/defining-social-innovation
[21] https://www.aa.org/
[22] https://www.ashoka.org/en-gb/story/experiences-scaling-impact-ashoka-globalizer-program
[23] https://www.inc.com/lindsay-blakely/patagonia-2018-company-of-the-year-nominee.html (Accessed 29 August 2019)
[24] https://ssir.org/articles/entry/whats_your_endgame (Accessed 5 July 2019)

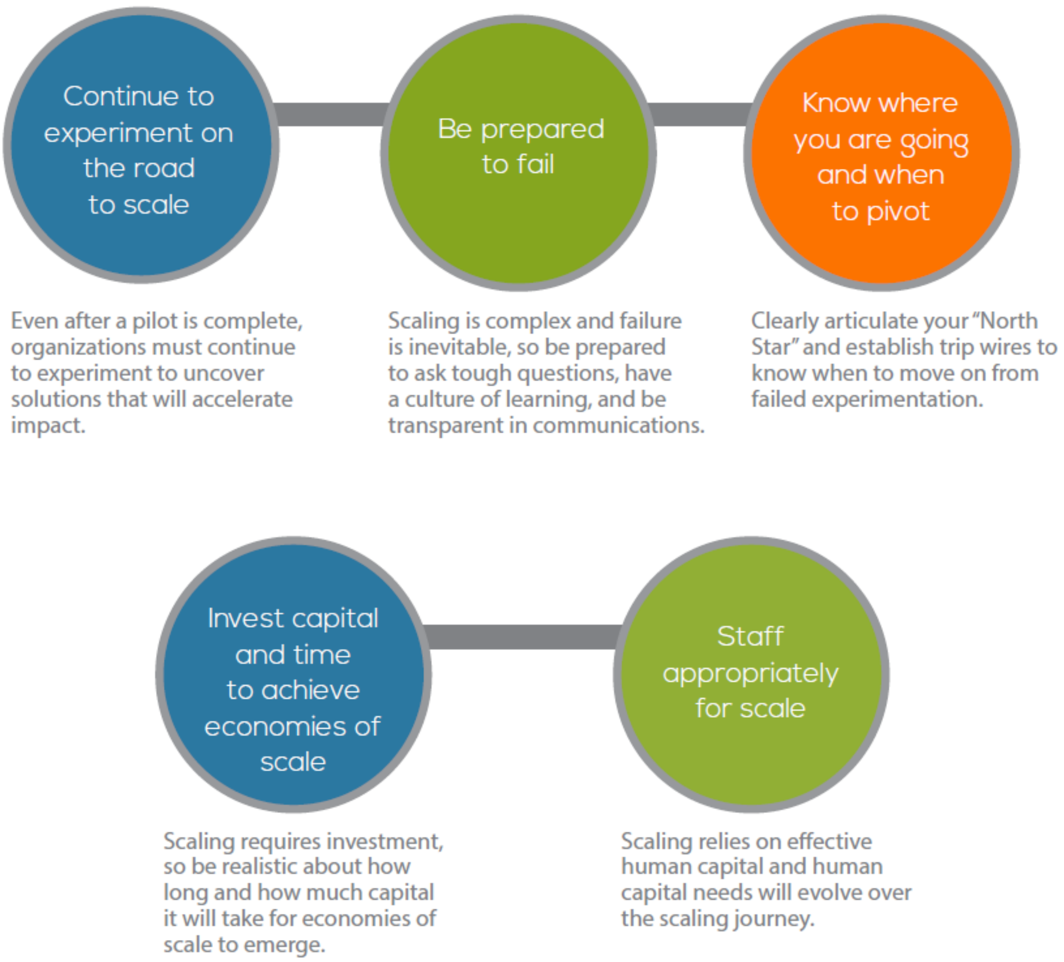
Case study: VisionSpring

Full case study available on the Scaling Pathways website:
https://scalingpathways.globalinnovationexchange.org/

Excerpt: "As a global non-profit organization, VisionSpring has worked for more than 15 years to create affordable access to eyewear, everywhere. While the mission has remained central, the strategies and business models used to achieve these goals have evolved radically over time. As is the case in many sectors, reaching impact at scale requires constant iteration and often involves pivots. When VisionSpring sought to scale its "Hub and Spoke" retail model across Central America, results were not as expected. After a promising start, net income was significantly lower than forecasted and impact among target customers was not scaling as planned.

"Ultimately, VisionSpring determined that its mission could be more efficiently and effectively achieved in other ways. The organization decided to end all Central American operations, return donor funding, and pursue exciting new scaling pathways. Along the way, it learned that the path to scale involves constant experimentation; preparation for failure is critical; knowing when to pivot relies on tripwires; reaching economies of scale requires investment and time; and scaling depends on the right staffing and skillsets."

Key Lessons:



Theory of Change

Some believe that an overhaul of capitalism is the only way to create a system that works for all: devolving wealth and power away from a few extremely wealthy individuals and very large organisations in one fell swoop. This is a lofty challenge, one that would be welcome but in practice, difficult to implement at a global scale.

I take a more pragmatic view in this paper. I believe the most likely way to change the system to one that is fairer, more inclusive and more equal is by using existing structures in better, more equitable ways.

It is rare to find early entrepreneurs working at a systemic level. To be able to influence a system, one needs a strong reputation, buy-in, networks, evidence and gravitas. This only comes with time and practical experience, and entrepreneurs usually only have the headspace to think about these higher goals once their models are sustainable. Only once businesses are at a certain scale can they then start to have systemic impact.

Ensuring more social enterprises reach scale, delivering balanced value to all stakeholders and demonstrating what's possible, will help to slowly shift the existing system.

The focus of this paper is to examine whether social enterprises – those businesses that ultimately exist to deliver a social or environmental mission alongside profit – can be significant in multiple sectors of the economy. There is a strong argument that the world would be a better place if it had a more balanced economy with more social enterprises operating at scale. How can we give social enterprises the best chance at reaching scale, both in their organisational size, but most importantly, their impact?

The Questions

The most basic question is how does society get back on track? How do we design and implement a new paradigm that doesn't, or even can't, allow greed to overrule? How do we ensure everyone has a fair chance at a happy and fulfilling life?

The hypothesis of this paper is that promoting social enterprise as the new paradigm will get us some of the way there. Its specific research questions are:

1. How are social enterprises actually doing as a sector, compared to commercial Small to Medium sized Enterprises (SMEs)?
2. What are the barriers and approaches to getting social enterprises to scale?
3. Should we take a more systematic approach to scaling social enterprises across sectors? Are there certain sectors where there could or should be more social enterprise activity?
4. What is a compelling yet stretching vision for the future? How can we organise support systems and different forms of capital to achieve that vision?

Context

This is the right time to be asking these questions, given the following contextual factors.

Mainstream recognition

More people and organisations are recognising the need to maximise more than just shareholder return – not only to ensure an everlasting and better world, but also because it makes financial sense in attracting the best talent, and managing risk.

In the report 'Scaling Impact: Blueprint for collective action to scale impact investment in and from Australia,' it states that "Communities and innovators are demanding more sustainable choices and products that are restorative and regenerative by design – shifting away from extractive models to a more circular economy." A few examples bring this to life:

> Almost 200 CEOs of US companies comprising the Business Roundtable signed a letter shared in the New York Times (Aug 19, 2019) declaring delivering shareholder value to no longer be their sole purpose; that they must also invest in employees, deliver value to customers and take account of all stakeholders.

> Larry Fink, CEO of BlackRock with $6.8 trillion under management, said: "Society is demanding that companies, both public and private, serve a social purpose."[25]

> Dutch pension fund PGGM, with over $220 billion in assets reported: We are convinced financial and social returns go hand in hand[26]

> 93% of C-suite respondents to a 2018 survey conducted with the Association of International Certified Professional Accountants endorsed the need for a wider view of value creation[27]

[25] https://www.blackrock.com/hk/en/insights/larry-fink-ceo-letter (Jan 2018)
[26] PGGM, Annual Responsible Investment Report 2017
[27] Association of Certified Professional Accountants and Black Sun Plc in association with the IIRC, Purpose Beyond Profit: The value of value – Board level insights, 2018

> Over 60% of millennials surveyed rate a sense of purpose as a major factor in working for their employer, 87% think corporate success should be measured by more than money and 86% report interest in sustainable investment[28].

Entrepreneur Motivations

The Global Entrepreneurship Monitor (GEM) UK report for 2017 looks at the motivations of entrepreneurs starting new businesses each year. In 2017, it created a new category to track called "creating meaning", such as helping others and making a difference to society. It finds two-thirds of women entrepreneurs motivated by improving society and 58% by helping others in need.[29]

	Male	Female
	%	%
To choose the people I want to work with	63.4	64.9
To continue a family tradition	13.7	21.6
To contribute to society	39.2	66.0
To build great wealth or a very high income	58.4	58.4
To fulfil a personal vision	69.4	79.7
To help others in need	38.2	58.0
To have good relationships with others	67.9	81.9
To build long-lasting relationships with others	62.1	72.8
To challenge myself	75.6	80.0
To be free to make my own decision	88.8	87.8

Table 2: UK motivations for starting a business by gender 2017 - percentage of Total Early-stage entrepreneurial Activity (TEA) entrepreneurs stating the motivation was fairly or very important (Source: GEM UK APS 2017)

What is a Social Enterprise?

Known as social enterprises, social ventures, profit with purpose, 'doing well by doing good', impact businesses, among many other names, these trading businesses have a mission, or purpose greater than maximising shareholder value, to improve the planet or the lives of people in need.

Unfortunately, there is no one generally accepted definition. Different agencies use different definitions (see Appendix I for a summary), making building movements around the concept of social enterprise difficult. It also complicates the experience for people and organisations wanting to support them by buying or procuring from them. The following characteristics are common to most definitions.

Mission

Mission is the most important defining factor of a social enterprise. It is their reason for existing: not to maximise profit, but to create positive lasting social or environmental change. Most definitions stipulate that this intent should be legally protected through a 'mission-lock'. Often this involves stating a commitment to having a social impact in the company's Articles of Association.

Trading Model

Not every social problem can be solved using a business model. Many problems will always rely on charitable giving or government intervention. But for those that can, business models help address problems in more long-lasting, sustainable and self-sufficient ways. A key tenet of social enterprise, agreed by most definitions, is the use of a **trading model**. There are a number of ways impact can be created through trading business models, and enterprises may choose to employ one or a combination of these impact models:

1. **Value proposition.** The product or service itself intentionally addresses a social or environmental challenge, often in line with one or more of the Sustainable Development Goals (SDGs) (e.g. education and care providers, housing associations, Polipop, HCT Group, social impact investing fund managers)
2. **Impact through Customers.** The product or service is purchased by low-income, vulnerable or disadvantaged customers, or with those groups as a key target customer segment among other segments. Products and services should be fair, available, affordable and accessible to all (e.g. Unforgettable, Fair For You, Base-of-Pyramid models).
3. **Impact through Employment.** A proportion of staff are comprised of vulnerable or disadvantaged people, with fair working conditions and benefits (e.g. auticon, Goodwill Solutions, Social Bite).

[28] Millennials, the Global Guardians of Capital, 2017, UBS; The Deloitte Millennial 2016 Survey, 2016 Deloitte; Morgan Stanley Sustainable Investing Surveys 2015 and 2017

[29] Global Entrepreneurship Monitor, United Kingdom 2017 Monitoring Report

4. **Impact through Supply Chain.** Ensuring fair pricing and safe working environments for social enterprise suppliers or vulnerable direct producers, or repurposing or diverting waste (e.g. Fair Trade, Café Direct, Rubies in the Rubble, Elvis & Kresse)
5. **Impact through Profits.** Surplus profit is reinvested into solving social challenges. This includes cross-subsidy models where profitable activities pay for unprofitable ones – 92% of social enterprises use the majority of their profit to further their social or environmental goals (e.g. Buy-one-give-one model like Toms Shoes or Stand4Socks, Equity for Good - Toast Ale). In addition, 12% gift profits to a separate cause (e.g. Belu Water) while 12% are the trading arm of a charity, returning its profits to the parent organisation (e.g. HCT Group).[30]

Legal Form

Organisations with "asset-locked" legal forms have restrictions on their ability to distribute any profits or other assets, and are often controlled by a regulatory body (e.g. Community Interest Companies, Charitable Incorporated Organisations (CIOs), charitable trusts, registered charities, and Industrial & Provident Societies). We refer to these throughout this paper as Regulated Social Enterprises – although not all organisations registered as one of the above will be a social enterprise. Traditional for-profit companies, legally registered as Companies Limited by Shares (CLS) in the UK, often have a harder time convincing social sector stakeholders they exist to create positive impact because of the lack of regulatory control on their activities. As mentioned, one way they can address this is by enshrining purpose, mission or operating principles in their Articles of Association.

Governance & Use of Profits

"Governance is the systems and processes concerned with ensuring the overall direction, effectiveness and accountability of a social or commercial organisation. For many social enterprises this role is taken on by a board of directors or trustees"[31]. Social Enterprises make decisions differently from commercial businesses. For example, they might decide to reinvest their profits into charitable activities versus paying out a dividend to shareholders, or hire people far from the job market at a higher cost and effort in order to achieve the goal of creating jobs for those groups of people.

Many definitions of social enterprise exclude businesses where 'private gain' may result from trading and investment, meaning individuals may stand to make a profit from its activity. Caps on profit distribution to shareholders can be used although this may hinder the ability of enterprises to raise capital from commercial investors. This is one of the most debated aspects to defining social enterprises.

Definition of Social Enterprise for this paper

All businesses exist to solve problems for people. Most start by identifying a problem and developing a solution that others will pay for. Social enterprises tackle the tough problems – ones that, if solved, have the potential to significantly improve the lives of people in need, or the planet. They address social challenges. Their most important stakeholders are the people whose lives they impact, not their shareholders.

It is important for social enterprises to act responsibly throughout all of their operations. Environmental, Social and Governance (ESG) factors are widely recognised considerations in measuring the sustainability and ethical impact of companies. This includes providing fair employment contracts and practices, diverse and inclusive policies, and a knowledge of and a commitment to reducing your environmental impact.

As stewards of impact and businesses with a mission to improve the world, who also set an example for how other businesses should operate, having strong ESG credentials is important. In fact, commercial investors now consider not having proper ESG policies and procedures in place as adding extra risk to their investments[32].

[30] SEUK State of Social Enterprise Survey 2017
[31] https://www.the-sse.org/resources/starting/how-to-establish-a-social-enterprise-board/
[32] https://impactalpha.com/as-assets-flow-to-esg-investing-investors-on-the-sidelines-face-hidden-risks/ (Accessed 23 April 2019)

This report uses the Social Enterprise UK (SEUK) definition of a social enterprise, but adds a requirement for those businesses to have proper ESG policies, practices and procedures in place.

> A social enterprise has the following common characteristics:
> - An enshrined primary social or environmental mission, through legal form, governing documents or ownership for instance;
> - Principally direct surpluses towards that mission;
> - Independent of government;
> - Primarily earns income through trading, selling goods or services; and
> - *Addition: Has a commitment to strong Environmental, Social and Governance performance*

Defining scale

There are a few well-recognised definitions of scale. The European Union defines a "small business" as having "fewer than 50 employees and either a turnover or a balance sheet total of up to €10 million" and medium-sized businesses as having "fewer than 250 employees and either a turnover of up to €50 million or a balance sheet total of up to €43 million".[33]

The OECD's definition of a High Growth Business specifies that "A firm is more than three years old, it has initial employment of 10 or more employees, and it achieves average growth of either employment or turnover of 20% per annum for three consecutive years." The Scaleup Institute also uses this definition to define a 'scaleup'.

Given those inputs, a working definition of scaled social enterprise, or social scaleup, for this paper is having turnover greater than £10 million, or having at least 50 employees.

When talking about social enterprises ready to scale, it is those with at least £1m turnover and annual turnover or employment growth of greater than 20% across three consecutive years, indicating ambition to scale and exposure to the stresses of building a high-growth business.

[33] http://ec.europa.eu/growth/smes/business-friendly-environment/sme-definition_en

Commercial vs Social SMEs

There are over 100,000 social enterprises contributing £60bn to the UK economy and employing two million people, according to SEUK's report: The Hidden Revolution[34]. When considering how social enterprises are doing at scaling, it is important to understand how they perform as compared to commercial SMEs. Are social enterprises really doing it worse than their commercial counterparts?

Number & Size

Unfortunately, there are many conflicting data sets regarding the status of social enterprise in the UK, making it difficult to make valid comparisons.

Given this context, in the UK:

> There were 5.7 million private sector businesses in the UK in 2018, 99% of which were SMEs.

> Of these, micro-businesses with 0-9 employees, comprised 5.4 million accounting for 96% of all businesses by number, but only providing 33% of employment and 21% of turnover overall.

> There are 210,000 small (10-49 employees) and 35,000 medium (50-249 employees) sized businesses in the UK, accounting for 3.7% and 0.62% of all businesses respectively.

> There are 8,000 large businesses (> 250 employees), accounting for 0.14% of all businesses by number (0.38% of VAT/PAYE registered businesses), yet providing 40% of employment and 48% of turnover.[35] This figure excludes central and local government, charities and other non-profit organisations, which would bring the total to 10,220.[36]

> There are 1,220 large Non-Profit or Mutual Associations.[37]

> 10% of SME employers are social enterprises, 16% are socially-oriented SMEs, and 5% are traditional non-profit organisations, while the remaining 69% are purely commercial.[38]

> There are 36,510 scaleups, employing 3.4 million people and contributing £1.3 trillion of turnover compared to £1.6 trillion for SMEs overall.[39]

> The Department for Culture, Media and Sport (DCMS) Social Enterprise Market Trends 2017 report found 99,000 employer Social Enterprises, as well as an additional 84,000 employer non-profits and 244,000 'Socially-oriented' employer SMEs, or mission-led businesses operating in the UK.[40] Socially-oriented businesses were defined as being for-profit companies with a social or environmental intent.

> However in 2016, Big Society Capital (BSC) and DCMS commissioned research, finding there to be 123,000 mission-led businesses, representing £165 billion turnover and 1.4 million employees. This research used a tighter definition looking at governance, business model, intent, and external perception.

[34] The Hidden Revolution, SEUK https://www.socialenterprise.org.uk/the-hidden-revolution (Sept 2018)
[35] Parliamentary briefing - Business Statistics, Dec 2018 https://researchbriefings.files.parliament.uk/documents/SN06152/SN06152.pdf
[36] https://www.ons.gov.uk/file?uri=/businessindustryandtrade/business/activitysizeandlocation/datasets/ukbusinessactivitysizeandlocation/2018/ukbusinessworkbook2018.xls
[37] Ibid.
[38] Longitudinal Small Business Survey 2017 - SME Employers, cross-sectional report https://www.gov.uk/government/statistics/small-business-survey-2017-businesses-with-employees
[39] ScaleUp Insights - ONS (March 2019) http://www.scaleupinstitute.org.uk/research/the-scaleup-landscape/
[40] Social Enterprise: Market Trends 2017, DCMS & BEIS https://www.gov.uk/government/publications/social-enterprise-market-trends-2017

> There are at least 3,000 medium-sized social enterprises, employing over 50 people[41] and thus meeting our definition of scale.

SEUK estimates there to be 5,000 large social enterprises, employing more than 250 people.

> "Our analysis of the data with regard to those CICs, CLGs and charities with employees suggests that around 4% of CICs, 9% of CLGs and 4% of charities with staff employ over 250 employees. If this is accurate, we can, for the first time, make a prudent assumption that around 5% of social enterprises have been discounted from previous research...[and] there would likely be around 5,000 large social enterprises not captured by the [Department for Business, Energy & Industrial Strategy] BEIS research."[42]

Taking a top-down view, this incredulously suggests that large social enterprises represent nearly half of the 10,220 large companies in the UK.

Some examples of groups that may make up this large raft of social enterprises include 211 Housing Associations with over £10m revenue (see later), delivering £20.3 billion turnover altogether; 115 Public sector mutuals, together delivering £1.6 billion turnover, and 763 Multi-Academy school Trusts, receiving £22.5 billion income.

Comparing sizes of commercial and social enterprises (see Figures one and two), there are no major differences in distribution. In fact, it appears there are more large social enterprises by proportion than commercial ones, both by turnover and employment.

Figure 1: UK Business Population by Turnover of commercial businesses versus social enterprises[43]

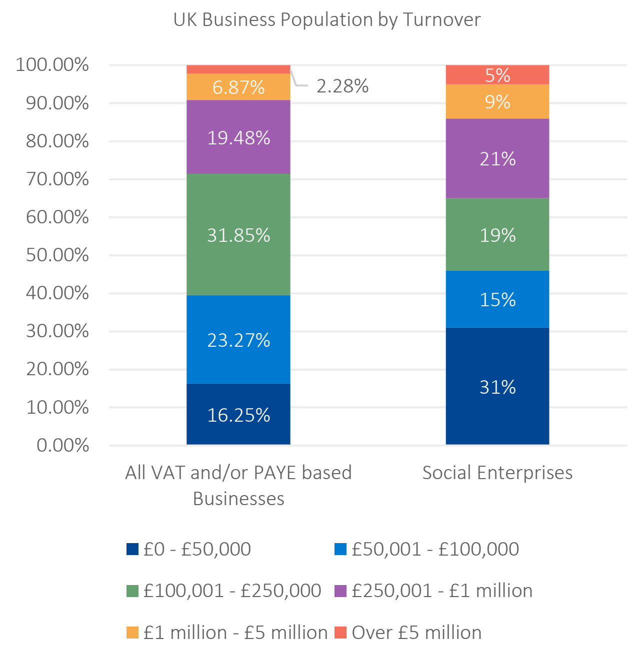
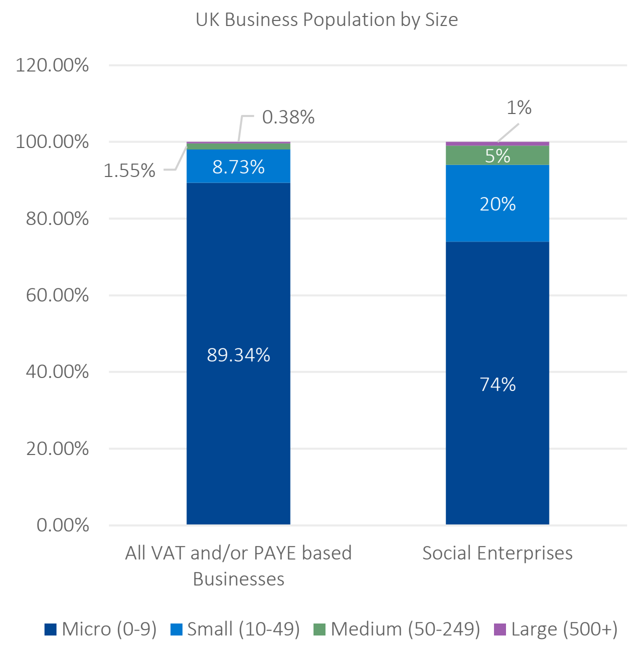


Figure 2: UK Business Population by Employment rates of commercial businesses versus social enterprises [44]



[41] Social Enterprise: Market Trends 2017, DCMS & BEIS https://www.gov.uk/government/publications/social-enterprise-market-trends-2017

[42] The Hidden Revolution, SEUK https://www.socialenterprise.org.uk/the-hidden-revolution (Sept 2018)

[43] UK SME data includes only those businesses that are VAT or PAYE registered, representing 2.6m businesses, or 45% of the total UK business population. https://www.ons.gov.uk/file?uri=/businessindustryandtrade/business/activitysizeandlocation/datasets/ukbusinessactivitysizeandlocation/2018/ukbusinessworkbook2018.xls
Social enterprises data The Future of Business - State of Social Enterprise Survey 2017, SEUK https://www.socialenterprise.org.uk/the-future-of-business-state-of-social-enterprise-survey-2017

[44] Ibid.

Age

Social enterprises are younger than commercial businesses, with 39% under five years of age versus 15%, and only 23% greater than 21 years versus 54% of commercial SMEs.

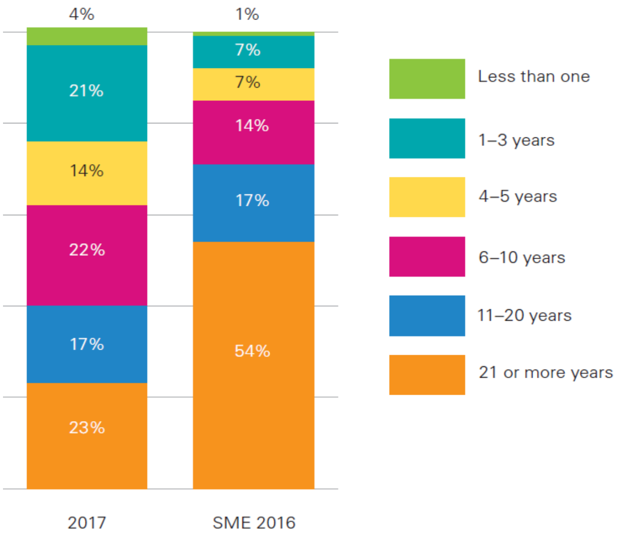


Figure 3: Length of Operation, SEUK State of Social Enterprise Report 2017

Sector

According to the Social Enterprise: Market Trends 2017 report, 32% of social enterprise employers are active in service sectors including education, health, arts and entertainment, 25% operate in the retail and distribution sectors, while a further 18% work in production sectors including agriculture, manufacturing and construction.

Social enterprise employers are less likely than SME employers to be operating business services (8% vs. 34%) and are significantly more likely than SME employers to be active in human facing social service sectors (31.5% vs. 8%).[45]

Areas of Deprivation

Social enterprise employers are significantly more likely to be located in the 20% most deprived areas than their commercial counterparts. One third of social enterprises are located in these areas compared to 13% of SME employers. However, social enterprise employers were less likely to be located in the second most deprived quintile of areas: 10% of social enterprises compared to 22% of social enterprise employers[46].

Profitability

Social enterprises are more profitable than commercial businesses. A lower proportion of SME employers had generated a profit over the last year when compared to social enterprise employers overall (76% vs. 93%)[47]. The sample of the BEIS data surveyed only 181 social enterprises, 44% of which were Companies Limited by Shares (CLSs). This is a very high proportion compared to 16% legally registered CLSs from SEUK's sample size of 1,581, and may explain these results.

This does infer that for-profit social enterprises may be more profitable than their commercial counterparts.

Growth

DCMS and BEIS report that the proportion of social enterprise employers (78%) that aim to grow is higher than the proportion of SMEs (63%). Of social enterprise employers aiming to grow, 39% are likely to approach external finance providers to help fund this growth, versus 22% of the commercial SMEs aiming to grow[48]. Once again, the high representation of CLS for-profit social enterprises in the research sample may explain this, as well as social enterprises potentially considering grant-makers as 'external finance providers'.

[45] Social Enterprise: Market Trends 2017, DCMS & BEIS https://www.gov.uk/government/publications/social-enterprise-market-trends-2017
[46] Ibid.
[47] Ibid.
[48] Social Enterprise: Market Trends 2017, DCMS & BEIS https://www.gov.uk/government/publications/social-enterprise-market-trends-2017

The amount of High-Growth SMEs is regularly tracked in data sets and surveys, but unfortunately not in the social enterprise market. It is important, however, to understand the composition of these firms in the commercial world, and their defining behaviours. The Longitudinal Small Business Survey (LSBS) 2017 is a large-scale telephone survey of 6,619 UK small business owners and managers[49]. **Eight percent** of panellist firms (those who answered the survey three years in a row) in the LSBS would be classified as high-growth on both the OECD turnover and employment definitions.

In the UK overall[50]:

> **Almost half of all start-ups do not make it to their third year**: 54.7% is the 3-year survival rate of UK-owned firms born in 2014 (and surviving to 2017)

> **Less than 2% get to the 'first million'**: 1.9% of businesses born in 2014 with turnover <£500k, survived to 2017 with £1m+ turnover – an early indication of scale.

> **It is slightly easier, but still difficult to grow past £1m:** 7.2% of businesses born before 2014 with £1-2m turnover in 2014 scaled to £3m+ in 2017

SEUK reports the following basic growth rate figures, compared below between social and commercial enterprises:

Table 3: Reported change in Turnover to previous financial year

	SMEs[51]	Social Enterprises (SEUK data)[52]	Social Enterprises (BEIS data)[53]
Increase	27.5%	47%	31%
No change	49.8%	30%	45.8%
Decrease	17%	20%	23.6%

Innovation

Social enterprises are more innovative than commercial businesses. Two-thirds (65.8%) of social enterprise employers reported introducing a new or significantly improved product or service over the past 3 years, a higher proportion than that for SME employers (42.5%). Almost half (48%) of social enterprise employers reported introducing a new process for producing or supplying goods or services against 19% of SME employers.[54]

Exporting

Social enterprises do not export as much as commercial businesses. A significantly lower proportion of social enterprise employers compared to SME employers exported their goods and services outside the UK in the past 12 months (27% vs. 17%).[55]

Customers

Social enterprises, like commercial businesses, have four main customer groups:

1. Business to Customer (B2C) – selling to the general public
2. Business to Government (B2G) or Business to Business to Government (B2B2G) – selling to government
3. Business to Business (B2B) – selling to private sector business
4. Third Sector – selling to other third sector organisations

A B2G or B2B2G business needs strong cross-party political connections, both to help sell services into government, but also to know in the first instance what's backable. Ark (see case study on page 85) was an early adopter of political innovation by delivering some of the first academies, and thus built a unique reputation and contacts within national government. Ark's political connections help them better understand which venture ideas may succeed or fail, and gives ventures they back

[49] The 2017 LSBS survey follows from the 2015 and 2016 surveys that had sample sizes of 15,502 and 9,248 respectively. The survey has a longitudinal tracking element, establishing a 'panel' of businesses that is re-surveyed in subsequent years, enabling a detailed analysis of how combinations of factors affect business performance through time.
[50] http://www.enterpriseresearch.ac.uk/wp-content/uploads/2018/06/2018-dashboard-master.xlsx
[51] Social Enterprise: Market Trends 2017, DCMS & BEIS https://www.gov.uk/government/publications/social-enterprise-market-trends-2017
[52] The Future of Business - State of Social Enterprise Survey 2017, SEUK
[53] Social Enterprise: Market Trends 2017, DCMS & BEIS https://www.gov.uk/government/publications/social-enterprise-market-trends-2017
[54] Ibid.
[55] Ibid.

access to government to have the right conversations to see if there is appetite for their proposed solutions.

According to various sources, fewer social enterprises (52%) employ B2B models than their commercial counterparts (71%), and tend to employ B2G (54% vs 43%) and third sector models (50% vs 34%) more. The Public Sector is the main source of income for 59% of social enterprises over £5 million turnover, 63% of which is from a local authority, 15% from local clinical commissioning groups and 6% from police and crime commissioners. In addition, 28% win contracts with central government, and 12% are benefiting from European programmes.[56]

B2B businesses tend to be more productive than B2C businesses. A study of American firms of all sizes found that value added per person in B2B firms in 2008 was around $120,000 per job, compared with $80,000 for B2C firms.[57]

Table 4: Source of income for social vs commercial enterprises

	SEs[58]	Employer SMEs[59]	Scaleups[60]
B2C	28% main model / 60% do some	64% do some (82% in London)	No data available
B2G	20% main / 54% some	42.7% do some	20% sell to local govt; 13% to national govt; 15% part of supply chain
B2B	14% main / 52% some	71% do some	55% sell directly into and 28% part of a supply chain for large corporates
Third sector	7% main / 50% some	34.1%	No data available

Access to Finance

Taking on external finance has been linked to business growth and performance. The LSBS shows a continuous decline, with 14% of businesses seeking external finance in 2015 falling to 9% by 2017, consistent across broad sectors and size-bands.[61] The four main reasons for applying for finance were the same for social enterprise employers and SME employers overall:

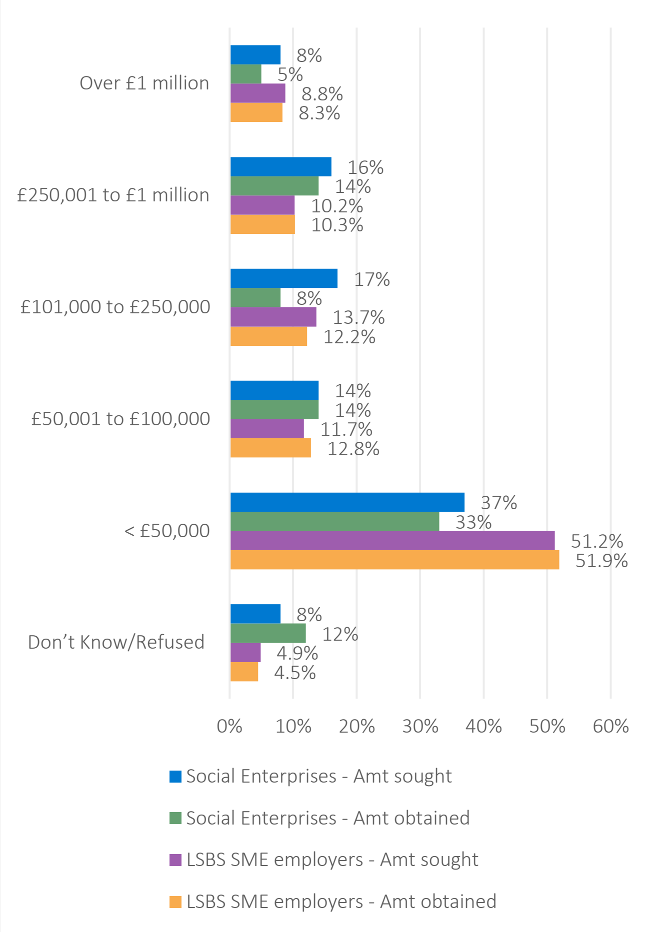
1. To acquire working capital or for cash flow reasons;
2. To acquire capital equipment or vehicles;
3. To buy land or buildings; or
4. To improve processes and products.

Social enterprises are very likely to apply for grant funding (82%) versus loan funding (24%) or equity funding (5%). More social enterprises are seeking greater amounts of finance than commercial SMEs. Social enterprises applied more often than SMEs for amounts between £100k and £1m. Social enterprises struggled more to raise amounts of finance between £100k and £250k, and over £1 million, as compared to commercial counterparts[62].

The Access Foundation makes repayable finance of up to £150,000 available for charities and social enterprises through a network of intermediaries. The data mentioned above was valid through 2017, just at the time when many Access Foundation Growth Funds were launching. At 31 December 2016, charities and social enterprises had received only £60k of investments, with a further £460k committed from Access funds. By December 2017, this had grown to £6.7m deployed into charities and social enterprises, increasing to £15.2m by the end of December 2018[63]. The amount of repayable finance available to charities and social enterprises has thus been significantly increased since the last SEUK survey, and we would expect to see a large increase in the amount obtained figures for <£50k and £101-250k as a result.

[56] SEUK State of Social Enterprise Survey 2017
[57] Spence M & Hlatshwayo S (2011) *The evolving structure of the US economy and the employment challenge Working paper*, New York: Council on Foreign Relations. Note: the study looked at firms of all sizes
[58] SEUK State of Social Enterprise Survey 2017
[59] Social Enterprise: Market Trends 2017, DCMS & BEIS https://www.gov.uk/government/publications/social-enterprise-market-trends-2017
[60] ScaleUp Institute: Annual Scaleup Review 2018
[61] Longitudinal Small Business Survey 2017 https://www.gov.uk/government/statistics/small-business-survey-2017-panel-report
[62] Commercial data from Longitudinal Small Business Survey 2017 - SME Employers, cross-sectional report; Social Enterprise data from SEUK State of Social Enterprise Survey 2017
[63] https://access-socialinvestment.org.uk/learning/quarterly-dashboard/ (Accessed 10 May 2019)

Figure 4: Amount of Funding Sought & Obtained by Social and Commercial Enterprises in 2017



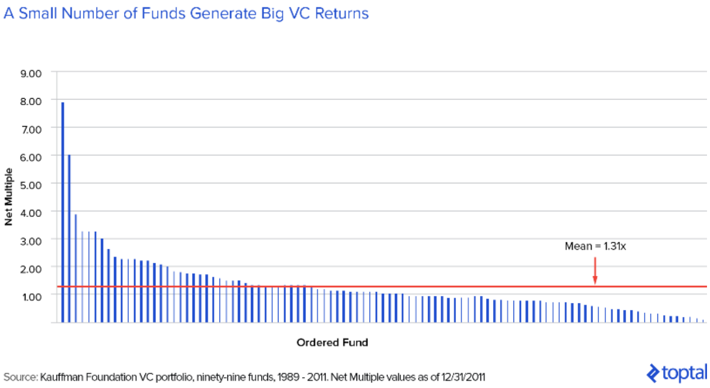
Equity Finance

Private Equity (PE) and Venture Capital (VC) play a key role in the British economy. In 2015, UK investment grew to just under £6 billion from £4.7 billion the previous year, with nearly 800 businesses receiving funding. From the LSBS, however, equity finance was used by only *2% of SME employers*. Of those taking on equity finance, 32% gained it from another business or organisation, 30% from within the company, 17% from family or friends, 14% from business angels, and 13% from a venture capitalist. **This means only 0.9% of SME employers use external institutional equity capital.**[64] The reasons for this are numerous, including reluctance to give up control and/or ownership of businesses, not having potential to deliver enough return to investors over the right timeframe, as well as geographic scarcity of investors and available funds.

But how necessary and successful is equity financing?

Equity finance is the most growth-friendly type of finance, given you don't have to "pay it back". You do, however, have to give up some element of control and upside through selling an ownership stake in your business. Investors are attracted by the potential of large returns, but by taking very high levels of risk, there is potential to lose their entire initial stake. Mainstream venture returns are low and subject to Power Law (only a low number of ventures and venture funds generate big returns), with the majority of funds losing capital – but some seeing significant returns.

Figure 5: Power law in venture returns



In Beauhurst's research 'Start-ups of yesteryear revisited'[65] they look at 1,155 private, independent UK companies which raised equity investment in 2011, and plot their successes and failures in the following years.

> 18% of these companies went on to complete a successful exit.

> 19% failed in some regard: 15% are now dead. A further 4% have entered "zombie stage", suggesting that they are undergoing noticeable difficulties.

> 10% failed to grow beyond seed-stage.

SEUK's research says that just 5% of social enterprises applied for equity finance in 2017, although does not report how many of those were successful[66].

[64] Longitudinal Small Business Survey 2017 - SME Employers, cross-sectional report https://www.gov.uk/government/statistics/small-business-survey-2017-businesses-with-employees

[65] https://about.beauhurst.com/blog/startups-of-yesteryear-revisited (Accessed: 14 Feb 2019)

[66] SEUK State of Social Enterprise Survey 2017

Scaleup Finance

There is very little information on the availability of finance for social scaleups. The Government's Patient Capital Review found that accessing long-term finance is difficult in the UK's under-developed and fragmented ecosystem, particularly for knowledge-intensive companies. Successful government policy interventions such as the Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCTs) helped develop a thriving start-up community. However, opportunities remain to develop some of these start-ups into large-scale businesses, where the proportion of UK start-ups that scale into large businesses lags significantly behind the US. The lack of capital, particularly for companies needing more than £5 million, forms one part of a negative feedback loop, together with historically low returns for venture investments, and low attractiveness of the UK market to top talent[67].

Around £3 billion of equity investment is deployed to scale-up businesses annually in the UK, including £400 million from the European Investment Fund (EIF), the vast majority of which is matched by private capital, and all of which may be at risk following Brexit. One limiting factor is that the UK has too few large VC funds. Venture funds of less than £200 million AUM are generally not desirable for institutional investors, who typically aim for much larger investment sizes.

All initiatives launched as a result of the Patient Capital Review should not only be made readily available to social enterprises, but also designed specifically with them in mind. See Appendix II for a list of actions resulting from the PCR.

Conclusions

In fact, and despite perceptions, social enterprises are numerous and appear to be performing better than their commercial counterparts. They are more profitable and more innovative, but do not export as much. They struggle to obtain the finance they seek, particularly in the amounts of over £1 million and between £100k - £250k, which has begun to be addressed by the Access Foundation's Growth Funds. M**ore support could be given to social enterprises to: expand internationally, and obtain amounts of finance over £1 million.**

SEUK's estimate of 5,000 large (>250 employees) social enterprises, and DCMS & BSC estimate of 123,000 mission-led businesses in the UK reflect a surprising amount of activity. **More research should be done to understand the nature and needs of mission-led business. More should also be done to promote this positive level of activity and support their continued growth.**

There is currently not enough robust data on the social enterprise sector as a whole with many data discrepancies between sources[68]. It is encouraging that the Government is carrying out regular research through its Social Enterprise Market Trends report however, **a key recommendation is to increase sample sizes in future reports to provide more statistically significant data.**

There is a concerning lack of data on High-Growth Social Enterprises, or on social enterprises using equity finance, which makes it difficult to see how they may or may not be performing comparatively in scaling up. Again, **more research to match what is already collected on commercial SMEs should be built into the Government's Social Enterprise: Market Trends future reports.**

It is hard for commercial scaleups to access finance, let alone social scaleups. The Patient Capital Review has led to certain actions taken by the government to address the lack of capital availability for commercial scaleups, including making changes to existing tax reliefs like EIS and VCT. The Social Investment Tax Relief (SITR), a tax relief supporting social enterprises, current open consultation is very welcome. **The government should evaluate all measures to ensure they are both equally applicable to and accessible by social enterprises.**

Given the large contribution to the UK economy from social enterprises, **governing policy for this sector, currently sitting at DCMS, should be moved to BEIS**. This would go some way to relieving the data inconsistencies and ensuring policies designed to benefit SMEs are equally benefitting social enterprises and enterprising charities.

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[67] HM Treasury Financing growth in innovative firms: consultation response (Nov 2017)

[68] The BEIS & DCMS Social Market Trends 2017 survey employed the approach, sampling strategy and telephone survey questionnaire used in the UK Small Business Survey (SBS) and included 1,233 business owners and managers as respondents, of which probably not more than 200 were social enterprises (max social enterprise base respondents in charts was 181). The SEUK State of Social Enterprise survey had 1,581 social enterprise responses gathered via telephone interviews and online surveys, primarily with the person in day-to-day control of the business or the person responsible for the business finances.

Finally, a key piece of learning from the Patient Capital Review that translates well to the social sector is to really back scale-ups “already receiving funding, in order to help them grow quickly, with less time spent raising capital and less pressure to exit early”. Government can help build the legitimacy of investing in social enterprises by better enabling investing in social funds. This could be done by earmarking a portion of the British Business Bank’s Patient Capital money for social enterprise focused VCs and funds; or making concessionary capital available to social enterprises, funded by further Dormant Assets money or the Shared Prosperity Fund. **Let’s back our winners properly.**

Barriers and Approaches to Scale

Now we know that social enterprises exist in numbers, and perform relatively well to their commercial counterparts – how can we better support them to scale up? What are the barriers that scaleups face, and which are specific to social scaleups? And what approaches are working?

Barriers to Scale

The UK is the third best place in the OECD for starting a business but only ranks 13th for business growth.[69] So what are the barriers to scale for social purpose organisations as compared to commercial businesses? We start by looking at barriers common to all businesses.

There has been a lot written about the barriers to scaling up commercial SMEs. Ten barriers were identified across multiple sources, set out in Table five below, ranked based on the importance and frequency the barrier was featured across those sources.

Some barriers are consistently seen as key. In almost every single list, access to top talent appears, usually in pole position. The people you employ can make or break your success, and having people who have already been through a scaling journey is critical. In particular, the skills needed across the different phases of growth include[70]:

Start-up	Crafting a vision, storytelling, prototyping, sales and marketing, developing customer-facing technology, financial modelling, and capital fundraising
Growth	*All of the above, plus:* Operations, processes, replication & standardisation, operational technology, back office and enabling-function development – particularly commercial finance, people management and development, governance
Scale	*All of the above, plus:* Internal communications, capital allocation, managing through others, leadership at scale, developing people without progression as a core driver

The next most important barriers were access to finance and inadequate infrastructure – both in terms of getting your own house in order such as your processes and systems, as well as the impact of external regulations and red tape on your ability to scale.

[69] http://images.connect.o2.co.uk/Web/TELEFONICAUKLIMITEDO2/%7b9c943ab5-1bea-4fde-98ba-2337fb932dcb%7d_O2_Seven_essentials_for_scale-up_ebook.pdf (Accessed 24 March 2019)

[70] Tom Ebbutt email, 26 August 2019

Table 5: Barriers most common to all enterprises trying to scale

Barrier	Description	Strategies
Access to talent	> There is a much smaller pool of talent with experience scaling up and exiting successfully > Eight out of ten ScaleUp CEOs identify this as their biggest challenge, particularly the social and technical skills of their workforce, their ability to recruit from overseas and having the talent to secure international business.[71] > Finding and retaining talent keeps 64% of Scaleup CEOs up at night[72] > Finding and keeping talent is a challenge that gets worse with time: 45% of later-stage entrepreneurs find accessing talent to be very or extremely challenging, up from 25% of early-stage entrepreneurs[73] > Staff recruitment and skills cited by 37% of SME employers as an obstacle to success[74] > Access to talent, an overall reduction in workforce and greater prevalence of zero-hour contracts were all cited as challenges by public sector mutuals[75] > A lack of local skills makes recruitment difficult - a main challenge faced by Growth Hub clients[76] > Low attractiveness of the UK to top talent[77]	> Focus on hiring quality people rather than speed: don't lower your bar because you need to grow faster. > Fire people. Just do it![78] > Value diversity and work with people who are different to you. > Have deep sector knowledge in your team.[79] > Plan hiring well in advance, devote strategic effort to recruiting, and sell jobs with a strong employee proposition.[80] > Improve value of mentors, advisors by using them to solve specific challenges.[81] > Develop coherent and well thought through people strategies.
Infrastructure	> There is a lack of incentive to take the risk of going for large tenders and contracts. Should a business scale up its team and systems before bidding or after winning? > "Preparing to scale increases organizational costs, as investments are needed to upgrade technology, hire senior-level talent, and improve infrastructure[82]" > Scaleups lack space to grow and digital capacity.[83] Lack of premises in which to grow is a challenge faced by Growth Hub clients[84] > Maintaining customer service standards keeps 63% of Scaleup CEOs up at night[85] > Regulations & red tape cited by 46% respectively of SME employers as an obstacle to success[86] > No one is funding getting systems, processes and organisational design ready to accept bigger contracts and new markets for social enterprises[87].	> Before scaling B2B businesses, make sure to build a repeatable sales process where you can consistently bring new customers in, and prove non-founders can sell by adding salespeople and making them productive in a predictable timeframe.[88]

[71] ScaleUp Institute: Annual Scaleup Review 2018, Top challenges listed by 514 scaleup CEOs http://www.scaleupinstitute.org.uk/scaleup-review-2018/
[72] https://www.home.barclaycard/media-centre/press-releases/Almost-six-in-ten-leaders-of-scaling-businesses-have-faced-a-moment-of-crisis.html (26 Feb 2019)
[73] Rippleworks, The Human Capital Crisis: How Social Enterprises Can Find the Talent to Scale http://www.rippleworks.org/human-capital-crisis/
[74] Longitudinal Small Business Survey 2017 - SME Employers, cross-sectional report https://www.gov.uk/government/statistics/small-business-survey-2017-businesses-with-employees
[75] Public Service Mutuals - State of the Sector 2018 report
[76] https://www.gov.uk/government/publications/evaluation-of-growth-hubs-pilot
[77] Patient Capital Review: Industry Panel Response https://www.gov.uk/government/publications/patient-capital-review
[78] https://firstround.com/review/give-away-your-legos-and-other-commandments-for-scaling-startups/
[79] Interview with Professor Haslam, Director of Owners Scaleup Program at IE Business School in Madrid https://intertradeireland.com/insights/blog/is-scaling-up-harder-than-starting-up/
[80] Rippleworks, The Human Capital Crisis: How Social Enterprises Can Find the Talent to Scale http://www.rippleworks.org/human-capital-crisis/
[81] Ibid.
[82] https://ssir.org/articles/entry/why_proven_solutions_struggle_to_scale_up#
[83] ScaleUp Institute: Annual Scaleup Review 2018, Top challenges listed by 514 scaleup CEOs http://www.scaleupinstitute.org.uk/scaleup-review-2018/
[84] https://www.gov.uk/government/publications/evaluation-of-growth-hubs-pilot
[85] https://www.home.barclaycard/media-centre/press-releases/Almost-six-in-ten-leaders-of-scaling-businesses-have-faced-a-moment-of-crisis.html (26 Feb 2019)
[86] Longitudinal Small Business Survey 2017 - SME Employers, cross-sectional report https://www.gov.uk/government/statistics/small-business-survey-2017-businesses-with-employees
[87] Interview with Devi Clark, Impact Hub Scaling Programme Manager (21 January 2019)
[88] https://www.innovationexcellence.com/blog/2019/04/02/the-missing-step-for-start-ups-who-want-to-scale-up/

Access to finance and risk capital	> There is a lack of capital availability in the UK, with historically low returns for venture investments[89] > Four in ten ScaleUp CEOs do not feel they have the right amount of finance in place to fuel their growth ambitions, with reservations about the use of 'unsuitable' equity finance[90] > Just 25% of public sector mutuals had reached their target investment figure in the past 12 months, with a disproportionate reliance on credit cards and grant funding[91]	
Access to markets	> Particularly the complexity of the procurement process and knowing about the right opportunities. In international markets, two key barriers are a lack of people experienced at winning overseas sales, and the inability to find appropriate overseas partners.[92] > Understanding new customers and markets is a main challenge faced by Growth Hub clients[93] > Routes for market access is a main challenge for Impact Hub members[94]	> It's easier to sell to an existing customer than to win new business. Make sure to balance the time spent chasing a new opportunity versus maintaining existing customer relationships[95]
Building leadership capacity	> ScaleUp CEOs want solutions for leadership development delivered at a local level, with peer-to-peer networks seen as most vital.[96] > A lack of leadership and management skills is a main challenge faced by Growth Hub clients[97] > Founder burn-out: 53% of founders say that building their business has been one of the toughest times of their lives while 25% say their mental or emotional health has been negatively affected but they've suffered in silence[98] > Leaders need to master finance to grow profitably: particularly cash management, budgeting and planning. Founding entrepreneurs may not understand the financials of their businesses well enough to scale up profitably. Some don't understand which product lines are loss-making if their overall position is break-even or slightly positive.[99] > A language or understanding barrier often exists that prevents people from finding the right finance and growth solutions for their businesses. Getting good finance people on board is crucial.	> Invest in teams, not just CEOs[100] > Work with Boards of directors to help them adopt new skills and mindsets[101] > Hire amazing leaders as early as you can and help grow their capabilities[102] > Grow leaders internally: it's hard to hire senior and middle managers, so make training and development a core competency[103] > Hire senior financial capability, like a CFO, to help make strategic decisions on what areas of the business to stop, start and continue
Strategy & Competition	> Standing out from the competition keeps 63% of Scaleup CEOs up at night[104] > The time for business owners to set aside to focus on growing a business, as opposed to managing the day to day operations of the business is a main challenge faced by Growth Hub clients[105] > Competition in the market cited by 51% of SME employers as an obstacle to success[106]	> Write down what you're doing in the world. What's your vision for the change you want to make?[107] (See Mumsnet case study on page 34 below)

[89] Patient Capital Review: Industry Panel Response https://www.gov.uk/government/publications/patient-capital-review
[90] ScaleUp Institute: Annual Scaleup Review 2018, Top challenges listed by 514 scaleup CEOs http://www.scaleupinstitute.org.uk/scaleup-review-2018/
[91] Public Service Mutuals - State of the Sector 2018 report
[92] ScaleUp Institute: Annual Scaleup Review 2018, Top challenges listed by 514 scaleup CEOs http://www.scaleupinstitute.org.uk/scaleup-review-2018/
[93] https://www.gov.uk/government/publications/evaluation-of-growth-hubs-pilot
[94] Impact Hub Global Impact Report 2018 http://impacthub.net/impact-report-2018/
[95] http://images.connect.o2.co.uk/Web/TELEFONICAUKLIMITEDO2/%7b9c943ab5-1bea-4fde-98ba-2337fb932dcb%7d_O2_Seven_essentials_for_scale-up_ebook.pdf
[96] ScaleUp Institute: Annual Scaleup Review 2018, Top challenges listed by 514 scaleup CEOs http://www.scaleupinstitute.org.uk/scaleup-review-2018/
[97] https://www.gov.uk/government/publications/evaluation-of-growth-hubs-pilot
[98] https://100stories.co.uk/proprietary-research/
[99] Interview with Hayley Hand, secondee at Social Business Trust, (01 April 2019)
[100] https://ssir.org/articles/entry/why_proven_solutions_struggle_to_scale_up#
[101] Ibid.
[102] https://firstround.com/review/give-away-your-legos-and-other-commandments-for-scaling-startups/ Molly Graham, ex-Google, ex-Facebook
[103] Rippleworks, The Human Capital Crisis: How Social Enterprises Can Find the Talent to Scale http://www.rippleworks.org/human-capital-crisis/
[104] https://www.home.barclaycard/media-centre/press-releases/Almost-six-in-ten-leaders-of-scaling-businesses-have-faced-a-moment-of-crisis.html (26 Feb 2019)
[105] https://www.gov.uk/government/publications/evaluation-of-growth-hubs-pilot
[106] Longitudinal Small Business Survey 2017 - SME Employers, cross-sectional report https://www.gov.uk/government/statistics/small-business-survey-2017-businesses-with-employees
[107] https://firstround.com/review/give-away-your-legos-and-other-commandments-for-scaling-startups/ Molly Graham, ex-Google, ex-Facebook

Culture	> Workplace culture is key! Of 40% of leaders hired externally each year, nearly half fail within the first 18 months (2014 CEB research).The main reason given for these high-profile exits is a poor fit with the team and the culture they encounter more broadly within the organisation[108] > Maintaining employee wellbeing and satisfaction keeps 66% of Scaleup CEOs up at night[109]	> Make a list of the qualities you want your company to embody. Who do you want to be? How do you want it to feel to work there? Prioritize principles over process[110]
Commissioning and procurement	> The greatest challenge for 40% of public sector mutual survey respondents; 34% also cited lack of capacity to win new contracts as a major issue.[111] > Complex procurement processes & how to find out about available bids[112] > Misaligned incentives and goals in public sector contracts. Not about small or big, can be at any scale.	> Structure is the issue: design contracts so everyone wins and everyone's goals are the same.
Communication	> As companies get bigger, more people need to be kept informed and communication becomes more challenging. The founder can no longer yell out a piece of news from their desk or put it out on IM to a small team.[113]	> Communicate your vision and strategy – over and over again. > Have processes to broadcast important information, collate feedback and answer questions
Ability to reinvent or adapt	> Businesses need to reinvent their models, and/or be able to adapt them to new contexts in new locales to scale effectively. This can be done deliberately before expansion, or reactively in the field.	> In analysing 45 social scale ups, Larson, Dearin and Backer (2017) found that dynamic change is a reality for successful [social] program scale ups. They found the programs evolve as leadership responds to opportunities to serve more communities and individuals.

[108] https://www.albion.vc/blog/your-business-fit-scale
[109] https://www.home.barclaycard/media-centre/press-releases/Almost-six-in-ten-leaders-of-scaling-businesses-have-faced-a-moment-of-crisis.html (26 Feb 2019)
[110] https://firstround.com/review/give-away-your-legos-and-other-commandments-for-scaling-startups/ Molly Graham, ex-Google, ex-Facebook
[111] Public Service Mutuals - State of the Sector 2018 report
[112] ScaleUp Institute: Annual Scaleup Review 2018
http://www.scaleupinstitute.org.uk/scaleup-review-2018/
[113] https://www.albion.vc/blog/your-business-fit-scale

Case study: Mumsnet

Mumsnet was conceived in early 2000 when Justine Roberts, founder, embarked on a disastrous family holiday. Her idea was to create a website where parents could swap advice about not just holidays but also all the other stuff parents talk about. Mumsnet is now the UK's biggest network for parents, with over 14 million unique visitors per month, £8.3 million in turnover and over 128 million page views. In their annual accounts, they say they "put purpose before profits and believe in listening, engaging and fearlessly standing up for our users' beliefs."

Justine was not able to raise money for many reasons, and consequently had to bootstrap the business for six pre-revenue years. She was determined to make the best site for those users who had supported it through thick and thin, rather than chase short-term metrics imposed by external funders. In retrospect, that turned out to be a good model for long-term growth.

> "As the team had grown, I hadn't properly communicated what made Mumsnet different. I had continued to behave as though we were all sitting around my kitchen table, picking up how to do things by osmosis. That's fine when you're five people, but not when you're 50.
>
> I realised that I needed to work at communicating our mission, vision and values, so that everyone could make decisions with those in mind. And it turned out to be liberating: it meant I could trust people to get on with it, get out of their way and stop being the bottleneck I was rapidly becoming. I also realised that I could hire people who were better than me; so long as I gave them a clear understanding of our goals and values, they'd go off and do a much better job than I ever could. This sounds obvious, but it's revolutionary when you're a bootstrapped founder used to doing pretty much every job yourself, from finance to marketing to product design."
>
> Justine Roberts, Founder of Mumsnet[114]

[114] https://www.telegraph.co.uk/women/business/mumsnet-founder-justine-roberts-scaled-start-up/

Barriers to Impact at Scale

Despite the many unique opportunities social scaleups have, they also face additional barriers to scale given their dual profit and purpose missions, legal forms, sources of finance and origins. Not all social enterprises face all of these barriers, but most will face at least one. Social-specific barriers are described in Table six below.

Table 6: Barriers specific to social enterprises trying to scale

Barrier	Description
Limited Market Sizes	> Selling to a tightly defined market, such as a population of people facing a specific vulnerability (i.e. the learning disabled in the UK) will limit the social enterprise's total available market, thereby limiting growth potential. > They often operate in areas of market failure, with a lack of other companies competing in that market. This can result in high costs of products for people, such as equipment for the disabled[115], to make the business work economically. > Social enterprises limited to public sector commissioning and procurement by selling outcomes like 'reduced homelessness' struggle to grow as their growth is ultimately determined by current political whims and ever decreasing budgets[116]. > In some cases, operating at scale might require diverting from the impact mission to make economics work. To reach a niche market of vulnerable customers, social enterprises might need to also supply mainstream markets. This may leave the business stronger financially, but susceptible to mission drift. > Therefore, are there ways to grow the addressable market while remaining on-mission? Increase your geographic reach might be one. Certified B Corporations are businesses that balance purpose and profit. In the US, they are legally required to consider the impact of their decisions on their workers, customers, suppliers, community, and the environment. Many successful B-Corps are B2C brands who serve the general population, appearing on supermarket shelves and retail shop racks, giving them a wide appeal, large market presence and unique ability to grow while still delivering impact at scale. Andiamo Orthotics makes high quality, custom fitted orthoses for disabled children, reducing the wait time from up to six months to one week. The data surrounding demand for orthoses is poor, as it is not collected regularly, however rough estimates say there are 2 million people in the UK requiring some form of orthoses[117]. Other data suggests children make up 10% of that demand[118], giving a TAM of about 200k children.
Increased operational cost and complexity due to their impact models	> Certain models of creating impact are more difficult to scale than others (see Table seven below for analysis). It is possible to scale when employing vulnerable people like the homeless, ex-offenders, and long-term unemployed people, but it becomes harder to compete with similar commercial businesses who do not bear the extra costs of specialised training and support. > The management and leadership skills to support a vulnerable workforce are tough to find and scale. And execution relies on getting the right workforce mix, which is constantly changing. > In supporting vulnerable people through a supply chain, such as subsistence farmers through Fair Trade, costs are higher but can sometimes be passed on to general public customers through good branding and a strong, fair proposition. > Low margins often results from higher operational costs and complexity, as well as not being able to charge higher prices to compensate for higher cost bases: some social enterprises will always deliver low margins. This is less attractive to commercial investors, both from a risk and return perspective. Social Bite is a movement to end homelessness in Scotland that started by running sandwich shops employing homeless people. In six years, Social Bite has gone on to employ 70 people, where 1 in 4 have struggled with homelessness, and operate a chain of five social enterprise sandwich shops across Edinburgh, Glasgow, and Aberdeen as well as a food catering and delivery service called "Social Bite Delivers". Its Social Bite Academy enables the employment of people affected by homelessness (32 in 2018) and supports homeless people to volunteer (45 in 2018). They realised

115 https://www.scope.org.uk/campaigns/extra-costs (Accessed 28 March 2019)
116 https://www.pioneerspost.com/news-views/20190220/we-need-talk-about-markets (Accessed 28 March 2019)
117 https://www.england.nhs.uk/commissioning/wp-content/uploads/sites/12/2015/11/orthcs-final-rep.pdf
118 https://www.cddft.nhs.uk/media/550993/01.17.09%20orthotics%20questionnaire%20attachment%201.pdf

the scale of the challenge of homelessness in Scotland was much bigger than what they could address through their shops alone, and have raised funds for other projects like a Housing First pilot and building a Social Bite Village, an innovative, low cost, safe living environment for up to 20 people for around 12 -18 months.

auticon is a multinational IT consultancy and social enterprise, which exclusively employs autistic adults as IT consultants. It actively markets the special skills of its consultants as its Unique Selling Point, to increase sales and help pay for the extra costs it faces in supporting its workforce. Started in 2011 in Berlin, auticon now employs more than 200 colleagues across the UK, USA, Germany, France and Switzerland with all 150 consultants on the autism spectrum. The team completes projects in software testing, development, analytics, compliance & security with clients ranging from major corporations (Experian, Linklaters, Channel 4, Allianz, etc.) to SMEs and start-ups. It has also achieved more than 50% year on year revenue growth, with current estimated revenues of $2.5m USD[119].
To support its consultants, auticon provides in-house job coaches who ensure that consultants' work environments enable them to deliver to their full professional potential. The job coaches prepare consultants for their prospective workplaces and brief them about specific corporate cultures; brief future team-members in terms of autism and any specific requests their new autistic colleague may have; offer initial support with travelling to and from work; facilitate reasonable adjustments; and mediate feedback between the client and the consultant.

Inability to attract and develop top talent due to low Sector Pay & inability to offer equity compensation

> Low sector pay and a lack of share options as compensation can make it difficult to attract top talent.
> Working in purposeful organisations often doesn't pay as well as commercial business: profit-making from social organisations is often considered wrong[120]
> Social entrepreneurship is a "Middle-class" activity due to the lack of meaningful salary for often long periods. This could be excluding the best ideas because of lack of resource and networks to bring to life[121].
> In addition, one's family background has an impact on their confidence to be an entrepreneur. In fact, it was recently found that "parental entrepreneurship and genes are the two most important factors generating sibling similarities in entrepreneurship"[122]
> Regulated social enterprises with no share capital also cannot offer any, performance-based or other, equity ownership to better attract top talent.
> Guilt over internal spending versus mission spending can mean a lack of investment in talent development. Also, if founders and management teams have never worked in large organisations, they may not have learnt what good learning and development looks like.

Perception of low quality coupled with less focus on branding and marketing

> Social enterprises have struggled with being seen as low quality, producing charity goods and services. This results in fewer corporates and government procurement departments willing to buy from them.
> Some social enterprises actively hide their social purpose as it's been shown to decrease sales. This may depend on the social issue, as some are more appealing to consumers than others.
> Also, the importance of hiring branding and marketing expertise is sometimes overlooked for more operational capability. First and foremost, the social enterprise must ensure its own sustainability by reaching and engaging customers successfully. The Social enterprise sector in general is very far behind its commercial counterparts when it comes to market research, and branding and marketing expertise.

Cafédirect "One of the main guiding principles for Cafédirect in the early days was that it had to shake the stigma associated with the poor quality 'charity products'. Consistent high product quality standards were seen by Cafédirect management as critical because its benchmark competition was viewed as mainstream brands such as Nescafé original, and Kenco medium roast. Since launch, Cafédirect has achieved this and has always been viewed as premium quality brand with retail prices 20-30% above competition throughout most of its brand lifecycle."[123]

Canvas Coffee runs a café in Portsmouth & Southsea train station used to help those in early recovery from drug and alcohol addiction develop skills and confidence to take next steps in their life through volunteer opportunities and barista skills training courses. They stopped talking about their social mission as it was shown to decrease sales[124]: "It's not something we hide, but it's also not something we particularly promote either".

[119] https://www.owler.com/company/auticon1 (Accessed 29 March 2019)
[120] https://medium.com/here-and-now/purpose-should-pay-928eb361f637 Jack Graham, 6 Feb 2019
[121] https://medium.com/here-and-now/you-dont-have-to-be-rich-to-do-good-but-it-helps-bff3132b597e Jack Graham, 29 Jan 2019
[122] https://voxeu.org/article/family-background-neighbourhood-effects-and-entrepreneurship (accessed 5 July 2019)
[123] https://dspace.lib.cranfield.ac.uk/bitstream/handle/1826/5402/Rise_and_stall_Cafedirect.pdf;jsessionid=A8A5B71BC63100B162F0EC17A0633373?sequence=1 (Accessed 7 March 2019)
[124] Ben Smith email, 2nd Sept 2019

	Belu Water: "Marketing and branding expertise is critical. Don't underestimate the power of a good, consistent brand message, which clearly articulates why you're better than your competitors, with impact and environmental credentials a core part of that offering" (See case study on page 39)
Competition policy (State Aid) issues	> State Aid can occur whenever state resources provide assistance that gives organisations an advantage over others. Foundations can grant any amount but government is subject to EU State Aid regulation. > Any below-market rate government support has to qualify under existing State Aid carve-outs capping amounts of support or under general block exemptions to do with the activity, such as SME access to finance.[125] Otherwise, support from any public body will need to be approved by the EU commission to show it doesn't distort the market. > There are EU carve outs at the micro enterprise level, but they tend to fall away at larger investment sizes. Therefore state aid is especially constraining for providing support to scale ups.
Lack of access to risk capital (e.g. equity, grant or concessionary finance)	> "If you're launching a business in a sector where there are significant upfront costs involved in getting your business to market or where significant short term losses are necessary to work out whether or not the business could be viable in the long term, you need to be able to spend lots of money. And if you're operating this business in an explicitly social way, you're unlikely to be able to offer investors returns that come anywhere near justifying their risk. You need a grant or an investment that's soft enough to almost be a grant"[126] > Growth needs flexible, long-term capital. That is currently only provided by equity and only companies limited by shares can raise equity; a barrier for legal forms who cannot. > Grant funders should increase funding amounts (to greater than $500k) to support growth and diffusion; act as long-term partners (>5 years), not just a funder; fund core costs; and take informed risks when deciding who and how much to fund - go bigger on riskier bets when they're ready to scale.[127]
Inconsistent service levels and slow-to-move due to dependency on volunteers or community engagement	> Many social enterprises rely on the power and goodwill of volunteers who believe in what they are trying to achieve. This can be extremely helpful to the bottom line, but can also be a risk in delivering inconsistent service and can prohibit fast growth. > It can also prohibit raising finance if commercial investors see over reliance on volunteers as a risk to a profitable operating model. > If a social enterprise is reliant on its local community, which includes many different characters, a unique mix of skills, and a sense of community engagement, it becomes less likely for there to be a will to scale beyond the community. It also takes a very long time to implement projects. Community pubs and shops across the UK are hyper-local businesses that rely heavily on local community-members for support in terms of volunteering hours, investment and patronage. Often used as community hubs, they can have significant impact in their local communities, but are rarely, if ever, scaled up to multiple locations.
Specific skills gaps	> There is a need to cultivate advanced managerial and systems-thinking skills in social enterprises to amplify the impact they are achieving and help them better achieve their missions. > Skills in systems-level thinking, designing partnerships, strategies for scale, and thought leadership become increasingly important in social enterprises versus commercial ones[128]. "By helping to build or shape a new market, a company can generate social impact that far exceeds its firm-level impact."[129]
Lack of incentive to scale	> Many social entrepreneurs are more motivated by impact than profit, thus may have less drive to scale up. For instance, some entrepreneurs care about having local impact, and may not want to grow beyond their communities. > Often the ambition isn't big enough when social enterprises are small, and they're constantly being told a small lifestyle business is ok. Small is beautiful, but it won't have large impact or change the system.[130]
Fame too soon	> Social entrepreneurs become heroes in the sector very early on; they spend a lot of time at awards shows and dealing with PR, less time running the business. > Too much "heropreneurship" – the sector should focus on growing what already exists, rather than idolising those who start new ventures.[131]

[125] https://www.gov.uk/government/publications/state-aid-the-basics
[126] https://beanbagsandbullsh1t.com/2018/12/28/cant-get-there-from-here/
[127] https://ssir.org/articles/entry/why_proven_solutions_struggle_to_scale_up#
[128] Ibid.
[129] https://www.omidyar.com/spotlight/how-do-we-invest-across-returns-continuum
[130] Conversation with Dai Powell, HCT Group
[131] https://ssir.org/articles/entry/tackling_heropreneurship Daniela Papi-Thornton 2016

Case study: FRC Group

FURNITURE resource centre
FRC GROUP
BULKY BOB'S

FRC Group (FRCG)'s vision is of a society where people can obtain good quality, affordable furniture without experiencing the devastating impacts of furniture poverty – no bed to sleep on or unmanageable debts. It campaigns to raise awareness of furniture poverty and create practical solutions to get furniture to people who need it.

Over the past 30 years, FRCG has employed all manner of growth strategies, from organic growth by increasing its customers, to acquiring commercial competitors and bringing them under the social enterprise structure, to launching new businesses, to re-purposing their skills, assets and networks to develop new and complementary services. It has annual revenue of about £8 million.

It has only been over the past three to five years, however, that they have purposefully built scalability into their growth plans following CEO Shaun Doran's scholarship at Harvard's Strategic Perspectives for Non-Profit Management course. Shaun realised that it is no more difficult to launch a scalable business versus a small, more local business. In fact, it is often easier to bring partners on board because people are more often drawn to ambitious ideas versus small, local, ring-fenced ideas.

Following that experience, FRCG was able to define a clear mission for itself: to reduce and ultimately eradicate furniture poverty. They identified ten items of essential furniture, with the number one priority being a bed. This led to them launching several new businesses, including Our House, a competitor to BrightHouse, which ultimately failed, and the 'Amazing Mattress' which is launching soon and completely cleans and restores good quality second-hand mattresses to saleable condition.

Some of their lessons learned include:

> **If you're going to launch something, put enough resource behind it**. Ensure you have enough resource to hire the right people. While Our House ultimately failed due to optimistic assumptions on customer conversions based on irresponsible lending practice data (i.e. extending loans to customers who cannot afford to repay) by their main competitor, BrightHouse, funders had backed a six-store pilot, with plans to expand nationally to 200 stores if successful. They hired two ex-directors of BrightHouse and secured a 12-month secondment from a Lloyds Banking Group Director as well.

- **Structure new scale-ups carefully to reduce the risk of their failure affecting the long-standing business or charity operations.** Although Our House failed, the understanding with initial funding partners was that their start-up loans would be written off in the event of failure, ring-fencing the rest of the Group to protect it.
- **Diversify your customer groups away from public sector**. FRCG has begun consciously developing businesses that aren't reliant on winning public sector contracts. As local government budgets have fallen away, conditions for their businesses which sell to Local Authorities have been torrid and turbulent. Spreading customer base widely among different groups helps FRCG manage their risk.
- **With a strong company culture, growth by acquisition can diversify customers, lower risk and protect margins**. FRCG has acquired three private companies to date, bringing them under its social enterprise structure and ethos. One was a private sector waste management company, allowing FRCG the opportunity to diversify its customer base in that sector away from the public sector. Another company was competing with FRC, driving pricing and ultimately margins down. Acquiring that competitor has allowed FRC to drive its surplus back up to reasonable and responsible levels. FRCG has worked very hard on its culture over the past 20 years, making mergers and acquisitions easier than in a commercial scenario where cultures aren't as clear or deeply ingrained.
- **Use your assets (skills, expertise and networks), and customer insight to identify new expansion products**. FRC sells hard wearing, utilitarian furniture into housing associations and local authorities. Given existing networks with clients, and knowledge of their needs, FRCG launched Buckingham Interiors, providing a range of furniture more focused on the look and design to the senior living market through the same clients.[132]

Case study: Belu Water

Belu is a UK based bottled water company. The company produces a range of carbon-neutral and ethically sourced bottled waters, and donates 100% of its profits to WaterAid, the international development charity determined to make clean water, decent toilets and good hygiene normal for everyone, everywhere within a generation. Belu does not currently have any commercial investors as it funds its growth organically by reinvesting surplus when needed.

It is an asset-locked social enterprise. Belu trades as a limited company with profit shares owned by The Belu Foundation that entitles it to receive all Belu's profits. The Trustees of The Belu Foundation agreed to enter into a partnership model with Belu Water Limited and WaterAid whereby all profits of Belu Water Limited are passed directly to WaterAid. In addition, the trustees also agreed to grant any monies The Belu Foundation receives by way of donations directly to WaterAid.[133]

Set up in London in 2004, by 2008 it was saddled with debts worth £1.9 million. Karen Lynch came on board as a marketing director, and within eight months was promoted to CEO to carry out a new business plan by pivoting away from low margin supermarkets and towards more lucrative hotels, restaurants and offices[134]. In 2017, continued growth of the business generated £809,000 net profit from just over £5.6 million of trading revenues[135] to pass to WaterAid. In total, Belu has passed £3,038,662 to WaterAid since 2011, transforming 202,577 lives with clean water, decent toilets and good hygiene. Belu is on track to donate a record-breaking £1 million in 2019[136].

[132] Interview with Shaun Doran, CEO FRC Group 13th March 2019
[133] Belu Water 2018 Impact Report http://www.belu.org/toolkit/#impact
[134] https://www.bbc.com/news/business-39513159
[135] Belu Water Directors' Report and Financial Statements For the Year Ended 31 December 2017, Companies House
[136] Belu Water 2018 Impact Report http://www.belu.org/toolkit/#impact

Key Lessons[137]:

> Belu is a business first and foremost. It needs to survive and thrive in a rapidly changing market in order to have impact. It is singularly focused on providing the right offer to its customers with top quality, and its impact follows.

> Marketing and branding expertise is critical. Don't underestimate the power of a good, consistent brand message, which clearly articulates why you're better than your competitors, with impact and environmental credentials a core part of that offering

> Belu works with partners throughout its supply chain and is therefore able to keep its headquarters lean and nimble with only nine full-time employees.

> A critical move for Belu was the pivoting away from low margin business model selling direct to consumers through supermarkets, towards a B2B2C model.

> Belu believes in recruiting the right talent, with the right networks and experience, to be successful. It isn't afraid to pay well to attract the talent it needs, and use other incentives, like providing flexible working tailored to individuals.

> Its environmental credentials are a key part of its proposition. It has reduced its carbon footprint by 50% since 2010 and is the first and only water brand to achieve the British Standard Institute's Independent Carbon Neutrality Standard, PAS 2060. More recently, customers are more interested in its sustainability credentials than its WaterAid donations.

> Belu has remained agile, flexible, and is constantly adapting to the market with its proposition. It can quickly pivot to a different offer, such as introducing the Belu Filter Initiative, a free filtration machine for restaurant and hotel customers in exchange for adding a £1 WaterAid donation to their customers' bills.

As their very nature is to create impact, a key consideration is to ensure impact grows at the same pace and quality as the business. Three more characteristics make it difficult to scale the *quality*, or fidelity, of impact while growing the size of organisation and its turnover. Often organisations face more than one of these barriers.

1. **Ineffective impact measurement, data collection and learning.** The ability to measure your impact, learn from it and implement changes to improve your performance is critical to scaling the quality of impact alongside business growth. Without understanding *how* a model creates impact, it is impossible to scale up while at the same time maintaining and improving impact quality and fidelity. Social enterprises need to understand what aspects of their models deliver impact and are therefore core before scaling to different geographies or target customer groups. This requires high quality impact practice and measurement, a strong data collection and analysis function, and a solid theory of change. Without it, not only will a scaled business not have the impact it should, but also accessing some social investors and philanthropists could become difficult. It should be noted that this challenge could be heightened by funders or investors who ask social enterprises to collect and report on impact metrics that the enterprise doesn't need. The Esmée Fairbairn Foundation and IVAR conducted research into this phenomenon, resulting in publishing six new principles for grant reporting[138].

"High-fidelity replication is hard. You have to do everything as well as the innovators did. You can't leave stuff out, make arbitrary changes to methods and procedures, or cut corners just because you didn't raise enough money. If you do it wrong, it may not work at all. Replication is both a science and a high art: You must be committed to and obsessive about the details".[139]

e.g. Evidence Action's Dispensers for Safe

[137] Interview with Kieran Whiteside, Belu Water 21st Feb 2019
[138] https://esmeefairbairn.org.uk/why-we-need-to-flip-the-model-of-grant-reporting
[139] Kevin Starr, Enough Innovation Already! SSIR April 6 2018 https://ssir.org/articles/entry/enough_innovation_already

Water (DSW) are a proven, innovative, and low-cost approach to increase rates of household chlorination, disinfecting drinking water against most bacteria including those causing cholera. Through a disciplined monitoring process, the Evidence Action team tracked key indicators to identify whether the chlorine was being used effectively. Evidence Action measured adoption rates as the percentage of randomly sampled households whose water tested positive for Total Chlorine Residual during unannounced visits. As DSW grew by installing more chlorine water dispensers, the rate of adoption dropped. This was due to a number of factors including dispenser hardware problems, ensuring a constant supply of chlorine, and ensuring local volunteers remained actively engaged in educating their community, dispelling myths, and ensuring chlorine was being used appropriately. They made the decision to stop growing wide (by continuing to install dispensers), and focus on increasing impact through increased adoption of the existing dispensers[140]

Case study: Living Goods

"Living Goods is a well-known social venture that fields an Avon-like network of dynamic village community health promotors. These promotors sell health products (including malaria and pneumonia treatments) door-to-door, doing health education and making clinic referrals all the while. The Living Goods model went through many iterations, working through core issues like supply chain logistical systems and the right basket of goods. It turned out that the most important they learned was how to hire and train great salespeople as health promotors. They eventually got it right: A big, expensive RCT showed that villages with a Living Goods health promotor had an astonishing 27% drop in child mortality.

Living Goods has grown to a respectable size, with 3,538 health promotors in Uganda and Kenya. However, for the model to achieve impact at real scale, others will have to join as replicators. There's a lot of interest, and Living Goods is involved with a number of would-be replicators. But there is one big catch: The Living Goods model is complicated. Its systems, talent, and overall management are world class. If you want to get the same results, you need to be serious about it. You need to invest what it takes to do it right.

BRAC— one of the best Big International NGOs (BINGOs) in the world—is serious about it and has worked closely with Living Goods in Uganda since 2007. They rolled out at a much bigger scale, and worked with Living Goods staff to capture all their innovations and iterations. Together BRAC and Living Goods cover a population of 6 million people.

Living Goods has now developed a state-of-the-art management platform that will help BRAC and other NGOs deliver the model at high quality. They've learned that you don't just share your model with replicators; you have to give them the systems that allowed you to deliver it. With that platform, Living Goods is working to refine its approach to replication partnerships so that the process requires a shorter, less-intense engagement but yields the same impact.[141]

[140] https://static.globalinnovationexchange.org/s3fs-public/asset/document/FINAL%20Scaling%20Pathways%20-%20Evidence%20Action%20Case%20Study%20(5.11.17).pdf?g6C69_hLxqxqWfLEMeQ5R4pyq5h9n8iS (Accessed 24 March 2019)

[141] Kevin Starr, Enough Innovation Already!, SSIR, April 6 2018 https://ssir.org/articles/entry/enough_innovation_already Photo: https://livinggoods.org/who-we-are/

2. **Dependency on individuals with unique expertise.** A key barrier to entry in commercial markets is specialised expertise and deep sector knowledge. Similarly in scaling impact, if the impact created is dependent on a few key individuals with skills, experience, a certain manner or personality and knowledge that is hard to find and train, it will be more difficult to scale the quality of impact as it grows. It will need to find ways to mitigate the dependency of certain individuals with excellent hiring practices and employee training programmes, adding significant cost.

Example: Jamie's Farm

Jamie's Farm is a 5-day residential programme for excluded youth combining farming, family and therapy. It is highly reliant on the unique skills of Tish Feilden, lead Therapist, who is a UKCP Registered Psychotherapist with over 30 years' experience of working with children in schools, residential settings, clinical settings and the community. Tish coordinates and leads on the therapy of each individual and group. Jamie's Farm operates five farm sites across the UK, and is aiming to reach 10% of children who would benefit from the intervention within five years. Given the highly skill-dependent nature of the intervention working with vulnerable children and youth, scaling rapidly is difficult. Jamie's Farm says, "we will never expand at a pace that will compromise our quality... We will grow organically and nurture key qualities so that every child who lives and works with us in the future gains the same outcomes, the same lifelong memories, as children have done to date."

3. **Intervention is one-to-one, face-to-face and/or intensive.** When impact creation requires intensive, often face-to-face support for people, scaling can become a challenge. To scale up, lots of people resource will be needed. In addition to building up a high head count, and as in the previous point, ensuring the right level of expertise of each individual staff member delivering a service is crucial and can be costly. Like in the Jamie's Farm example above, the children have positive outcomes from physically being present at the farms, interacting with animals and benefitting from personalised therapy. Delivering this type of intervention at scale would require a lot of capital to ensure the fidelity of the model for each child participant. Other than building up head count, social models requiring this level of intensity could also seek to develop innovative approaches to find alternative resources to leverage.

Example: On Purpose

On Purpose works with inspiring professionals and helps them become leaders who put purpose before profit. It runs two programmes, a CEO programme, and an Associate programme in London, Paris and Berlin. Cohort sizes have an effect on the learning outcomes, group dynamics and enjoyment of Associates – smaller cohorts offer Associates, for example, greater interaction with guest trainers. As such, entry to each programme is capped at 20, with two intakes per year per city. In addition to its small staff team, On Purpose has built up a network of over 1,000 volunteer trainers, mentors and coaches with whom it has collaborated to develop its 500+ participants to date. It is considering how to make use of what it has built through its core programme to launch new and more scalable products like web-based learning platforms and online communities

This final barrier in particular poses a risk: do all social scaleups need to be tech-based, and have broad rather than deeper, more life-changing impact? Different impact models have qualities that may make it easier or more difficult to scale up. As mentioned previously, social enterprises may choose to employ one or more of these to create impact.

Table 7: Impact Models and Scale

Impact Model	Pros	Cons
Value Proposition The product or service is intrinsically impactful	> Lock-step model where impact increases as revenue grows > Potentially lower costs of raw materials, if recycling or reusing inputs	> May prove difficult to scale if dealing in a localised context e.g. community pubs and shops > The economics and market could be difficult
Impact through Customers People purchasing the product or service face a disadvantage	> Lock-step model where impact increases as revenue grows > Meeting a market gap: providing essential goods and services to people who may never have had appropriate access	> Potentially limited market sizes if target group is niche > Potential to abuse customers with unfair pricing: ethical standards of trade must be strongly upheld > Risk of mission drift: product targets mainstream customers rather than vulnerable customers.
Impact through Employment Employees of the social enterprise face a disadvantage	> Providing employment often results in deep impact, or significant change, for people who struggle to find employment	> Non lock-step model: need to balance ratio of vulnerable to non-vulnerable staff > Often has greater costs than competitors
Impact through Supply Chain Fair pricing and safe working environments for suppliers or vulnerable direct producers, or repurposing or diverting waste	> Lock-step model where impact increases as revenue grows	> Unless protected (either in mission-lock, Articles of Association, or branding), fair procurement principles could change > Could be difficult to procure and set up supply chains quickly that meet customer demands and requirements (i.e. high quality, timely and large production)
Impact through Profits Surplus profit is reinvested into solving social challenges.	> Potential to unlock large amounts of cash and in-kind donations for needy causes	> Non lock-step model: amount of donations, whether nominal amounts, or proportion of sales or profits, can be changed > Usually not contributing to any sort of systems change - general consumers may not be aware of / care about donations

Interestingly, only the value proposition impact model is intrinsically immune to mission drift. In all other models, the impact can be weakened. Vulnerable customers can cease to be one's target market, vulnerable employees can slowly over time comprise a lower proportion of staff, profits can be donated at lower proportions based on external and business factors that can all be justified. Does growing to scale then inherently threaten these models more? It is worth considering how mission drift can be structurally prevented when scaling businesses employ these four models.

Support Programmes

We now know what barriers scaleups face. How can we best support them to overcome these? Four behaviours were identified in the LSBS to have a positive effect on the chances of a business being a high growth firm:

> Businesses that have innovated products or processes were 13-16% more likely to achieve subsequent high growth,

> Use of external finance increases the probability of high growth (in turnover) by 12%;

> Use of business support increases the probability of high growth (in turnover) by 14%;

> Businesses providing staff training are 31-45% more likely to subsequently achieve high growth.[142]

[142] Longitudinal Small Business Survey 2017 https://www.gov.uk/government/statistics/small-business-survey-2017-panel-report

Supporting business to cultivate these behaviours would be a good start. There are commercial organisations who do this already. The ScaleUp Institute regularly maps the landscape of existing scaling support programmes in the UK and reviews their efficacy. It finds 219 programmes, a third of which are co-funded by the European Regional Development Fund and are therefore at risk given Britain's coming exit from the EU. They find significant gaps in programmes addressing access to talent and access to markets. Other findings include:

> Very few purely scaleup or scaling focused interventions with clear regional and local gaps

> More than half focusing on leadership development, peer networks or leadership capacity building.

> Only 10% designed to help scaleups to access public or private procurement.

> Only 7% offering office space or hubs that focus on the needs of scaleups[143].

In addition to this research, the ScaleUp Institute annually reviews and endorses exemplar support programmes, endorsing 39 UK programmes and identifying a further 10 as 'ones to watch'. These are categorised as providing support for talent and skills (7), leadership (13), access to markets (4), finance (16), or infrastructure (9).

Most of the programmes providing support for talent and skills are working with young people in schools and colleges to develop the right skills early in life. This is worthy, however does not meet the demand of scaling businesses today to attract and retain the right talent. In fact, none of the programmes endorsed fill this particular role. As they note, support accessing talent remains a gap.

In addition, the programmes providing infrastructure support mainly provide office space, hubs and co-working spaces, as well as access to research facilities, technical expertise, mentorship and peer-to-peer groups. They do not, however, appear to provide hands-on scale-readiness support in selecting and implementing bespoke systems, and codifying policies, processes and procedures that has been identified in this report as critical.

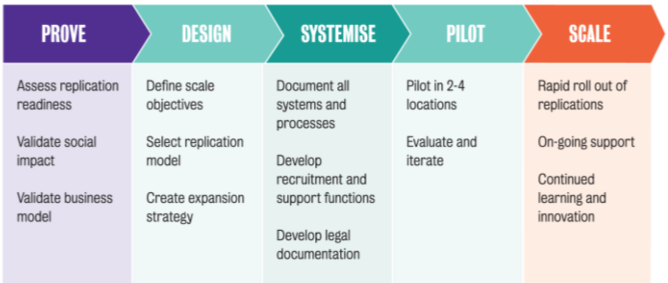
None of the programmes endorsed by the ScaleUp Institute address the barriers unique to social enterprise such as impact management, and limited market sizes. There are social sector equivalents who have done this for social enterprises – giving them support specifically to see them scale up.

Spring Impact – Scale Accelerator

Spring Impact, formerly known as the International Centre for Social Franchising, aims to help 30 social innovations scale by 2024. In 2015, it launched the pilot Scale Accelerator with the aim to support promising social enterprises to replicate and scale the proven impact of their programmes. Over nine months, each organisation receives a package of individual support and group training. To date, Spring Impact has worked with 17 organisations that deal with a range of issues from homelessness to youth leadership. Scale Accelerator will provide four more cohorts of social enterprises with support to scale their impact, thanks to £1.5 million of funding from the National Lottery.[144]

Spring Impact publish their Toolkit, and their five-stage process to scale.

Figure 1: Spring Impact's 5 Stage Process to Scale



In the first stage, Prove, scale-readiness is assessed in detail. In Design, businesses develop their strategic goals for scale, as well as their business model to enter new markets. Systemize consists of codifying the operations of the model and any supporting systems. In Pilot, the focus is on testing and improving the strategy and business model. The final stage, Scale, focuses on increasing the rate of scale: bolstering economies of scale, standardizing operations further, and quicker

[143] ScaleUp Institute: Annual Scaleup Review 2018 http://www.scaleupinstitute.org.uk/scaleup-review-2018/

[144] https://www.springimpact.org/2018/12/international-centre-social-franchising-now-spring-impact-2/

iterations on the business model.[145] Unfortunately, little is published about the evidence of how well this approach has worked so far.

Social Business Trust

Social Business Trust (SBT) supports high growth potential social enterprises to scale-up their impact by investing cash grants and professional support from their business partner organisations. Of the 1,000 social enterprises they reviewed, 22 were selected to receive over £15 million in cash grants and in-kind support over seven years. On average, beneficiary numbers double in the first two years after a social enterprise works with SBT[146]. They note in their 2017 report, Unlocking Growth, their key success factors to scaling social businesses:

1. "Set your boundaries: Be **clear on what your central purpose is and your chosen path for expansion**. Have a clear vision, understand your strengths, know your competitors, and don't get distracted. Say no to expansion opportunities if it stretches you too far.
2. "Have a clear roadmap, but **be flexible if circumstances change**: develop a summary strategy that outlines your ambition, where you want to play, how to win, and your priority top four actions.
3. **"Listen to your Customers**: know your customers and beneficiaries, get lots of honest feedback especially from customers you've had problems with. Use your impact reporting to improve your services.
4. **"Make Governance Matter**: Take time to think about the support and expertise you need from your board and then invest your energies into finding it. Recruit an excellent chair, strong board with the right skills and expertise you need,
5. **"Invest in your core**: Hire great people with specialist expertise to build an outstanding management team. Make sure your systems and processes are fit for purpose."[147]

Impact Hub Scaling Programme

Impact Hub Scaling was a program that supported 100 social entrepreneurs to scale-up nationally or internationally through eight Impact Hubs across Europe (Amsterdam, Athens, Bucharest, London King's Cross, Madrid, Milan, Stockholm and Vienna). Over one year, a team of mentors supported entrepreneurs to acquire the skills they need to successfully scale their enterprise, drive social innovation forward and create positive impact.

Each Impact Hub engaged with scaling managers, who had local knowledge and were able to help social enterprises identify territories in which they could scale across Europe through joint venturing, expanding and social franchising. The program also gave social enterprises the opportunity to acquire skills, knowledge, advice and access to investor networks by partnering with business experts in all eight cities. It also offered mentoring and tailored scaling support to address the needs of each selected social enterprise.[148]

Some of the key lessons from this programme about scaling are:

> **There are three phases to scaling up**: Scale-readiness; Market Research to understand where you should go and who to partner with; and Market Entry.

> **Get the organisation's systems ready for scale: Scale Readiness**. Most businesses had the desire to scale but weren't ready. There is a key distinction between the product being scalable and the organisation being ready (e.g. having the right systems and processes in place to be able to deal with being a lot bigger). This means buying and implementing a real CRM system rather than an excel file, writing your processes into an operations manual with training to accompany it rather than relying on employees knowing a process. It took the Impact Hub team between six and 24 months to put that in place, after which the businesses grew rapidly.

[145] Spring Impact - Five Stages of Scale Report, March 2018
[146] http://www.socialbusinesstrust.org/SBT_IMPACT_REPORT_2017.pdf
[147] http://www.socialbusinesstrust.org/SBT_Unlocking_Growth_Interactive_Version.pdf
[148] https://scaling.impacthub.net/

> **Scaleups don't see the value in scale-readiness… so dress it up as sales.** Ventures pay for accelerator programmes because they see them as an avenue to sales. But the real value is in the scale readiness work packaged up alongside potential customers.

> **Understand the true cost of expansion**. A scaleup needs to be able to separate out their headquarters costs, and location-specific costs to understand how the business model might work elsewhere. This allows a business to know how much each new location will cost.

> **Hire function specialists who are better than you are**. When a company is very small, employees will be doing everything. When scaling up, people need to adapt their roles. Leaders need to be willing to lead and manage in different ways, and employ people that are more expert than they are across different functional areas. As Molly Graham, ex-Google and Facebook, now COO of Quip, says, you need to Give Away All your Legos: "at a scaling company, giving away responsibility — giving away the part of the Lego tower you started building — is the only way to move on to building bigger and better things".

> **Scaleups needs more personalised attention than start-ups**. Start-ups are generally similar, and benefit from generic business support. Scaleups need bespoke support for the areas in which they may uniquely struggle – often sector-based nuances.[149]

UnLtd Big Venture Challenge

UnLtd's Big Venture Challenge (BVC) supported 120 social entrepreneurs with clear potential to scale, 74 of whom raised investment on or after the programme. Funded by the Big Lottery Fund, BVC was set up in 2013 to help early stage social ventures scale their impact. It provided intensive growth support and helped social entrepreneurs access investment of between £50,000 and £250,000, traditionally a level of finance that social ventures had struggled to access. In 2016, over 1.24 million people benefited from the collective work of the BVC ventures. They raised over £8.5 million in investment to match £4.5 million of funding from UnLtd. On average, each venture supported 684 more people a year after UnLtd's support, and grew their revenue by over £300k.[150]

The results? Of the 120 ventures supported, 92% continue to trade while just over 13%, or 16 ventures, are successfully scaling[151]. David Bartram, Director of Ventures at UnLtd, outlines several key learnings:

> **""Teach a person to fish": Focus first on growth not investment** – BVC began with the sole focus of helping ventures raise investment. We shifted this to a focus on growth and supporting the venture's business model (weaving together revenue, impact and scale) and sustainability. We learnt to focus on the resilience, operational stability and robustness of the business. Gearing a business up for growth was the aim, whether through replication, new contracts, new markets, or 'simply' sustainability. The support had to be tailored and focused on proper operational support, governance, impact measurement, systems and processes, sales strategies, not simply a business plan and financial model geared for investment.

> **"Support needs to be tailored** – by the time the ventures had got to BVC they had already been on multiple support programmes. Offering them vanilla workshops on 'measuring impact' or 'marketing' was relatively meaningless. When ventures are at the brink of growth, they need tailored, relatively sophisticated hands-on support to meet their needs. So we built a support model that combined in-house expertise with a tight network of trusted partners for more specialist advice (e.g. legal, branding).

> **"Early stage investment is not meeting demand** – the investment market is currently not meeting the needs of those that want to take on investment. We know there is a gap in the market when it comes to early stage social investment:

> > ***"There is a lack of appropriate or affordable capital*** – investor expectations of time horizons, appetite for risk, return and

[149] Interview with Devi Clark, Impact Hub Scaling Programme Manager (21 January 2019)
[150] https://www.unltd.org.uk/our-support/past-programmes/big-venture-challenge
[151] David Bartram, UnLtd interview 19 Feb 2019

entrepreneur skill set are not meeting the demands of the market. We found that funding of between £50k and £150k is rarely affordable, flexible or patient enough.

> *"There is a lack of capital for non-asset locked social ventures* – the 'institutional' market is often unable or unwilling to look beyond the ventures' legal structure. As such, it is skewed to providing capital (mainly debt) to organisations with asset locks (charities and CICs). We had to attract angel investors to back our 'profit with purpose' ventures, which were also those delivering the greatest growth in impact.

"Due to the need to balance social and financial returns, social ventures typically take longer to develop and grow compared to their more commercial counterparts. The investment market is not yet able to absorb the higher costs and risk associated with these business models. BVC was able to use grant money to offset this risk to ensure these ventures were able to take on the capital they needed to grow. This type of blended offering still doesn't exist in the market.

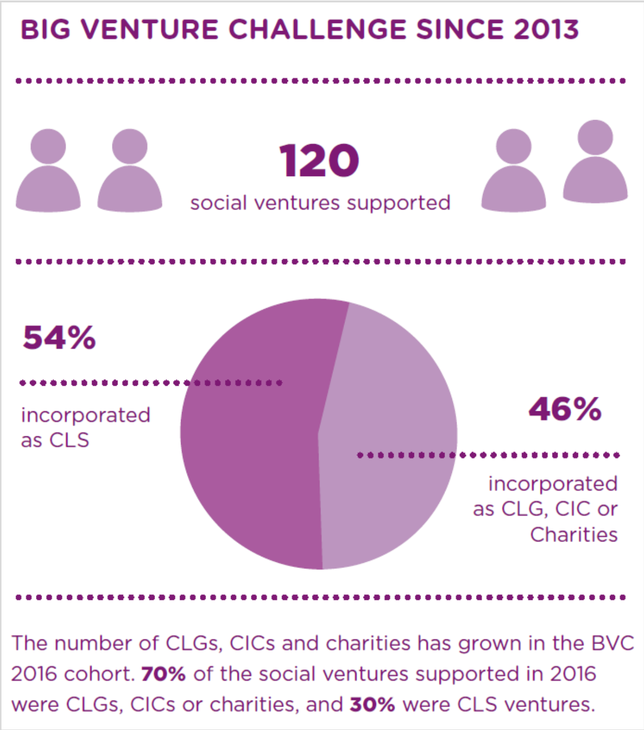
> "Vital support needed to prepare ventures for investment and engage with investors – there is a need to help social ventures navigate and engage with the social investors. Early stage investors are operating at such tight margins they cannot themselves support ventures to get ready for investment. The market is not able to pay for this – support organisations need to be funded to do this. For us, this has had to be funded philanthropically.

> "Post investment and longevity of support is crucial – there needs to be a shift away from 'programmes of support' to offering capital and support that is flexible to the needs of the entrepreneur and venture. This is especially apparent with post-investment support of those with ambitious growth plans. There is a lack of that type of support in the market.

> "The stage and type of venture is important to pick – identifying the stage of the venture's development is vital. Too early and they wouldn't make the most of the hands-on support.

> "Focus on business model not legal structure – we also took the decision to focus on a venture's impact, mission and leadership, not on legal structure. Our evidence shows us that the more commercially established entities (CLS) created more impact over the following 3 years than those who were asset locked. They were able to grow more quickly by accessing more finance, and they tended to be hungrier for wider and more far reaching impact."

Profit with Purpose



BVC note that profit with purpose (those with a Companies Limited by Shares legal form) ventures in the BVC programme had more impact than regulated organisations. Interestingly, the group of profit with purpose businesses in the BVC portfolio supported 2,826 more people a year after UnLtd's support, versus 686 average across the whole portfolio.

Between 2013 and 2016, social ventures taking part in BVC raised £8.6 million in external risk capital. Of that total, the 38 CLS social ventures raised £6.1 million – almost three quarters of the total and more than twice the amount raised by all other legal structures combined. CLS ventures raised on average £160,000 of external risk capital compared to an average raise of £71,000 per non-CLS structure.[152]

Based on their learning from BVC and built around the needs of the entrepreneur and their ambitions for scale, UnLtd launched a next accelerator programme, Thrive. This programme gives social ventures access to a consultant and bespoke support for six months to help reach scale. It will support 25 ventures per year across two focus areas: improving access to employment for those distant from the labour market, and developing products and services for an ageing society.

Asda's Social Enterprise Supplier Development Academy

Asda, in partnership with Social Investment Scotland (SIS), launched the Social Enterprise Supplier Development Academy in 2016. Funded through the proceeds of Asda's carrier bag charge, in 2017 the Academy supported 15 social enterprises from across Scotland, England, Wales and Northern Ireland to strengthen their understanding of supermarket retail and refine their commercial and marketing skills, with the potential to get their products on supermarket shelves. The programme included everything from understanding consumer purchasing behaviour, product trends, and supermarket logistics to branding and packaging design.

Asda no longer sell single use carrier bags in Scottish stores, so the exclusive partnership ended. Replacing the programme is the new Retail Academy with continuing sponsorship from Asda and support from the Scottish Government. A key lesson is providing a route to market for social enterprises, with introductions to potential corporate clients critical to helping them compete and win in commercial markets.

Approaches to Scaling

What are some of the approaches and routes to scale that actually work? Nesta's Making it Big Report says that developing a scaling strategy involves establishing why, what and how you're going to scale. The first step is to clarify social, organisational and personal goals for scaling; always being clear on what is fixed and flexible.

Next establishing what you are going to scale is critical. Is it all projects, or just a winning business line? Will one scaled up programme pay for the rest, or will you need to ditch some loss-making or non-impactful programmes? [153]

Once clear on aims, routes to scale become important. There are eight main ways of scaling social ventures, each with their own opportunities and challenges. The choice of approach will depend on the business, sector, and revenue and impact models. See Table eight below for a view on their pros and cons.

1. *Bottom-up / Organic Growth*: solutions to local problems coming from the community (often not designed with scale in mind). Focus on supporting existing small and medium sized social enterprises with Scale-Readiness support, access to markets and finance, and developing new product and service lines using their strengths and existing assets.
2. *Top-down*: take a large intractable social problem and design a purposely-scalable solution (e.g. Shift design, Zinc).
3. *International scaling*: Bringing successful foreign models to the UK and adapting them for UK context, or scaling British organisations internationally.
4. *Mergers or JVs:* combine two organisations who are trying to achieve the same thing into one or create a partnership through a Joint Venture (e.g. Ambition School Leadership as a merger between Teaching Leaders, Institute for Teaching, Future Leaders)
5. *Acquisition (or "Take social"):* Purchasing existing social enterprises, or commercial businesses (such as family businesses with no successors) and turning them into social enterprises; or finding an exit for your social enterprise by being acquired yourself.
6. *Franchising:* Licence your business' expertise, processes and brand to grow by other people
7. *Spin-outs*: Social intrapreneurs spinning out social enterprises from existing large corporates and governmental organisations (i.e. NHS)

[152] UnLtd Spotlight Paper - Purpose, Growth, Impact. Mission Locks Insights from Practice, April 2017 https://www.unltd.org.uk/uploads/general_uploads/UnLtd-Spotlight-Purpose-Growth-impact-Digital.pdf

[153] Making it Big: Strategies for Scaling Social Innovations, Madeleine Gabriel, Nesta 11 Jul 2014 https://www.nesta.org.uk/report/making-it-big-strategies-for-scaling-social-innovations/

Table 8: Approaches to Scale and their pros and cons

Approach	Pros	Cons
Bottom-up / Organic Growth	> Solutions more likely to work in a local setting, as designed with local context in mind, with deep impact. > Passionate local social entrepreneurs are inspiring, and driven by local impact > No fundraising stress > Would create real legacy and hero businesses for the UK, with deep histories	> Hard to scale out. Ideas may struggle to work in different contexts. > Often different people with commercial skills are required to get to scale, driven a little more by profit. Passion may get lost. > Takes a long time > Likely to be capital intensive, if not a tech-based business > They might not have scaled yet for reason that is difficult to address: small market, lack of demand
Top-down	> Solutions designed specifically to address a challenge, giving a greater chance of sustainable, scalable impact	> Hard to scale - like any start-up. Hard to find risk capital to grow, hard to prove business model, grow customers, etc. > May struggle to adapt to local contexts, depending on social challenge, thereby delivering less impact than expected. > Will likely require systems approach, and external actors, over whom you have little to no influence, to change to realise the impact.
International Scaling	> Solution (demand and willingness to buy) proven in other markets, less risk > Operational models, back end tech platform already exist if consolidate local market first	> Potentially difficult to adapt to UK context > Critical to find right local partners and channels through which to expand.
Mergers or Joint Ventures	> Increased resilience through diversifying income: reducing over reliance of each organisation on large contracts > Increased economies of scale	> Capital and time intensive > Risks around changes to culture, leading to unhappy staff and potentially losing great staff
Acquisitions	> Proven economic model, profitable business, established customer base therefore less risky	> Capital intensive > There are only so many ways to 'insert' impact in the model (e.g. workforce, profit treatment, governance) > Not designed to solve a specific social problem, so likely limited impact. > Lack of large social acquirers, making it difficult for social enterprises to exit while preserving mission. > Might be difficult to change culture of for-profit business staff to be mission- driven
Franchising	> Less capital intensive to open new locations as franchisees invest themselves > Quicker to scale up > Franchisees bring in fees and royalties, more financial stability	> Less control: rely on franchisees to implement properly > Having too many franchisees becomes hard to manage - ideally want franchise partners who will run 3-7 branches. > Need to have more than just one or two franchisees to retain power. > Upfront cost to codify your model > Less room for change and innovation
Spin-out[154] (e.g. Public Service Mutuals, Intrapreneurs, Betapreneurs)	> Backed in early (expensive and risky) stages by large organisation > Potential to launch speedy beta versions of products and services > Entrepreneurs benefit from market and network experience, resulting in greater market orientation and shorter time-to-market	> Risk of over reliance on one large founding client > Could be more focused on uses already seen in the industry in which they operate

[154] https://www.viasarfatti25.unibocconi.eu/notizia.php?idArt=18862 (Accessed 26 Jan 2019)

Case study: Groupe SOS, France

Case study from: OECD Policy Brief on Scaling the Impact of Social Enterprises: Policies for Social Entrepreneurship (Luxembourg: Publications Office of the European Union, 2016)

Created in France in 1984, Groupe SOS is now one of the largest social enterprises in the world. It has gradually widened its scope of action to the fight against social exclusion. Groupe SOS now numbers 350 different structures (NGOs, commercial enterprises, co-operatives) and operates in multiple sectors – ranging from childcare, senior care, care for the handicapped and healthcare to social housing, catering, transport, fair trade and communication, as well as services for people suffering from addictions and HIV/AIDS. Groupe SOS entities employ a total of 14,000 individuals and supports more than 1 million beneficiaries each year in France and 20 other countries.

In 2015, the group generated €700 million in revenues, mostly stemming from contracts with the public sector (75 % in 2013). Other revenue sources include partnerships with the private sector (€1.1 million in 2011) (OECD and Centre d'analyse stratégique [CAS], 2013) and consumer payments. Finally, Groupe SOS receives government subsidies (representing less than 1% of the total budget), as well as some project-related grants from the European Social Fund. Like other social enterprises, Groupe SOS has specific governance rules, including regulated salary scales, an absence of shareholders and non-redistribution of profits.

Scaling strategies: Groupe SOS bases its growth primarily on economies of scale, M&A and diversification. In 1995, Groupe SOS decided to pool several functions (accounting, legal services, finance, and human resources) within an "economic interest grouping", resulting in optimised resources and management processes. It simultaneously expanded by acquiring other social enterprises, which were either in financial difficulty or simply seeking to grow through shareholder participation. Groupe SOS also diversified its activities by creating innovative responses to numerous social issues.

In order to scale up the impact of social enterprises in France and around the world, Groupe SOS has developed two specific programmes: "Social Novation" and "Ambassadeurs Solidaires".

The *Social Novation* programme, co-funded by the European Social Fund, follows a three-step process: identifying a market niche and social needs that have not yet been addressed (based on interviews with local stakeholders), enhancing the impact of existing solutions or creating new ones when needed, and sharing the results of the process with the relevant stakeholders. This open source initiative aims to facilitate exchanges between professionals (associations, public authorities, and partners) in different fields, within and/or outside Groupe SOS, by organising multidisciplinary working groups.

The *Ambassadeurs Solidaires* programme sends Groupe SOS ambassadors around the world to establish partnerships with local actors and share their expertise on scaling social enterprises. [155]

Lessons: Groupe SOS illustrates the capacity of social enterprises to scale up through the years by combining multiple innovative scaling strategies – such as organisational growth, M&A and diversification – across multiple locations. The success of Groupe SOS can also be explained by its ability to identify unmet social needs and diversify its financial resources.

For further information, please see: http://www.groupe-sos.org/en; http://www.groupe-sos.org/actus/2402/Ambassadeurs_solidaires

[155] The programme has been implemented so far in 12 large cities: London, Milan, Mumbai, Singapore, Montreal, New York, San Francisco, Sao Paolo, Seoul, Hong Kong, Buenos Aires and Cape Town

Approaches in Practice – Lessons

What lessons can be drawn from the high-level approaches that have worked?

Organic Growth: Corporate Supply Chains

Through its flagship Buy Social campaign, and its Buy Social Corporate Challenge, SEUK hopes to support social enterprises into the supply chains of large corporates. Launched in April 2016, a group of over 15 high-profile businesses from a range of industries are aiming to collectively spend £1 billion with social enterprises. The Challenge's Year 3 impact report shows that as of April 2019, £65.2 million had been spent by corporate partners and the Challenge had directly or indirectly created 637 jobs at social enterprises.

Lesson: Supporting corporates to identify and procure from social enterprises is critical to growing market share for social enterprises. This helps social enterprises grow organically.

Top Down: Housing Associations

Housing associations are not-for-profit organisations that own, let and manage rental housing. Any surplus rent revenue is used to maintain existing housing and to help finance new homes and cannot be used for personal benefit of directors or shareholders. They can therefore be classified as social enterprises, although many do not identify themselves with that definition.

Housing associations established in the 1970s and 80s were funded by the Housing Corporation, which provided grant funding and took charges over the housing stock directly.[156] There are now 1,426 registered non-profit social housing providers in the UK[157]. Of those, 229 own more than 1,000 units, and have a combined annual turnover of £20.5 billion. There are 211 that meet our definition of scale with over £10 million turnover, with 55 of them having individual turnovers of over £100 million.

Lesson: Grants can play a catalytic role to getting social enterprises to scale and sustainability.

Spin-Out: Public Service Mutuals

The government defines a public service mutual as an organisation which:

1. has left the public sector (also known as 'spinning out')
2. continues to deliver public services and aims to have a positive social impact, and
3. has a significant degree of staff influence or control in the way it is run.[158]

There are now approximately 115 public service mutuals across England, delivering an estimated £1.6 billion of public services across the health sector, education, employment and skills and youth services. These businesses are often employee-owned, and profitable with over 92% of them making a profit in their last year. They are growing, by on average 50% since launch, and 7% in the most recent financial year, with turnover averaging under £15.5 million, and £10.2 million in their first year trading.[159]

Lesson: Launching with assets and long-term, established contracts with trusted counterparties can catapult a social enterprise quickly to scale. The key is to ensure to win further contracts quickly to reduce dependency on a single counterparty.

[156] https://www.wrighthassall.co.uk/knowledge/legal-articles/2016/04/28/brief-history-nearly-everything-about-social-housi/ (Accessed 3 May 2019)
[157] https://www.gov.uk/government/publications/current-registered-providers-of-social-housing
[158] https://www.gov.uk/guidance/introduction-to-public-service-mutuals
[159] Public Service Mutuals - State of the Sector 2018 https://www.gov.uk/government/publications/public-service-mutuals-state-of-the-sector-2018

Conclusions

There are many barriers common to all scaleups, the most important being access to talent (specifically with experience of scaling), building strong infrastructure and access to finance. Social enterprises also face unique barriers, both to grow commercially but also in maintaining the quality of their impact as they scale.

Many can be addressed through non-financial support, including designing coherent and robust people strategies, peer networks, leadership development opportunities, and access to sector-specific mentors and networks. Secondments from senior finance experts, or sales and marketing specialists can be very useful. Other barriers require capital to be addressed, such as funds to purchase and implement bespoke systems, as well as funds to hire the best talent.

"Scale readiness" has been cited by most scaling programmes to be of utmost importance – over and above getting ventures ready for investment by giving them business plans and financial models. **To reach the goal of more social scaleups, scale readiness support is a crucial ingredient.** Businesses should have a few full-time staff dedicated to 'how will we scale' – have a scaling division, or a chief scaling officer.[160]

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[160] https://ssir.org/articles/entry/to_impact_millions_the_social_sector_needs_to_scale_scaling_up (Greg Coussa, Jan 24 2019)

Sector View

We have explored how to build social scaleups by identifying the barriers they face, looking at existing support provision and what approaches work best to achieving scale. Are there certain sectors that may be more suited to larger social enterprise? Where might social enterprises have a competitive advantage? Where might the margins be high enough to support impact creation?

Part of this research involved a detailed sectoral analysis (see Appendix III: Detailed Sector Analysis) to see if any may be more or less attractive to social enterprises. It looked at the suitability of sector for social enterprises based on data from publicly listed companies in each sector, looking specifically at:

> Profitability: Net Margins, Return on capital

> Barriers to Entry

> Buyer & Supplier Power

> Existing social enterprise activity & potential competitive advantages

> Sector trends in high-growth commercial companies

Macro Trends

Macro trends need to be taken into consideration when thinking about where social enterprises should play an outsized role in future. Some of the most relevant trends to this challenge include:

1. **Brexit**. Regional funding for SMEs will be lost as Britain transitions out of the EU. Replacements for this funding need to be designed now, so as not to leave a massive funding gap for early stage businesses and scaleups.[161]
2. **Changing Demographics**. "There will be about 1 billion more of us by 2030, and we will live longer. The fastest growing demographic will be the elderly, with the population of people over 65 years old at 1 billion by 2030.[162]"
3. **Climate Change and the Just Transition**. "The climate will continue to change quickly and feature regular, extreme weather everywhere[163]"California's largest utility was overwhelmed by rapid climatic changes as a prolonged drought dried out much of the state and decimated forests, dramatically increasing

[161] ScaleUp Institute: Annual Scaleup Review 2018, p221
[162] https://sloanreview.mit.edu/article/the-world-in-2030-nine-megatrends-to-watch/ (Accessed 8 May 2019)
[163] Ibid

the risk of fire. PG&E was forced into bankruptcy, citing an estimated $30 billion in liabilities and 750 lawsuits from wildfires potentially caused by its power lines. [164] Conscious shifts to low-carbon, smart, decentralised energy system are starting to happen.[165]

4. **Tech Disruption** Opportunity as well as scepticism and ethical issues with emerging deep technologies like Machine Learning, Artificial Intelligence, Big Data and Robotics.[166]
5. **Resource scarcity.** Water scarcity as a pressing issue affecting industry, agriculture and becoming a much more expensive resource.[167]
6. **Data and Transparency.** Individuals are ever more aware of and concerned about the use of their data. While consumers request more transparency from companies, they demand more security for their own data. Data breaches pose a large risk to any business working with sensitive or large amounts of personal data.
7. **Circular Economy.** Facebook reports seeing buying patterns reflecting more conscious values, which includes people seeking new ways to extend the life cycle of their products and wardrobes.[168]
8. **Influencer marketing.** Millennials and members of Gen Z are growing up thinking of themselves as brands, using social media to promote their curated identities and finding ways to monetize their selfies.[169]
9. **Millennials wanting to work for companies with a mission**. Millennials are putting a greater emphasis on finding meaning and social purpose through work. But that doesn't mean they are necessarily entrepreneurs. We have a duty to create larger orgs to give people better employment opportunities, managerial positions.[170]

Appendix III: Detailed Sector Analysis for more detail)

In each of these sectors, high-potential existing social enterprises should be identified and

10. **Shift of focus to preventative healthcare** given the needs of an ageing population, and increasing costs of treatments and technologies.[171]
11. **Hyperconnectivity.** Billions of people now live in a networked world - n fact, anyone with web access can now access much of humanity's collective knowledge at minimal cost.[172]

Priority Sectors for the Social Sector

Considering all the analysis, seven sectors appear to have outsized potential for scaling up social enterprises. Sectors with large amounts of existing social enterprises were given an extra point to ensure the weighting for this characteristic was necessarily strong. From the table below, the list of priority sectors for social enterprise scaleups in order is:

1. Education
2. Housing / Homebuilding
3. Retail: Grocery & Food
4. Regional banks / finance
5. Green & Renewable Energy
6. Recreation
7. Healthcare

Sector	Profitability	Competition (1= very competitive)	Expected Growth	Barriers to Entry (1 =low/no barriers)	Buyer Power (1 =high buyer power)	Supplier Power (1=high supplier power)	Existing SE Activity (1= low activity)	Trends Risk (1=high risk)	Total
Education	1	3	3	3	2	3	4	3	22
Homebuilding	3	2	2	2	1	3	4	3	20
Retail (Grocery & Food)	1	3	3	1	1	3	4	3	19
Banks (Regional) - credit	3	2	2	3	2	3	2	2	19
Green & Renewable Energy	2	2	3	2	2	1	4	3	19
Recreation	2	2	3	3	1	3	2	3	19
Healthcare Products, Services and IT	2	2	2	2	3	2	4	1	18
Utility (Water)	3	3	1	2	3	3	1	1	17
Publishing & Newspapers	2	2	2	3	1	3	2	2	17
Drugs (Biotechnology)	3	1	3	2	1	3	1	2	16
Drugs (Pharmaceutical)	3	1	2	1	2	3	1	2	15
Telecom (Wireless)	1	3	3	1	1	2	1	3	15
Environmental & Waste services	1	2	2	3	1	1	2	3	15
Telecom Services	2	2	1	1	1	3	1	3	14
Real Estate (Operations & Services)	3	1	1	3	1	1	2	2	14
Insurance	2	2	1	2	1	3	1	2	14
Utility (General)	1	3	1	1	1	3	2	1	13
Farming & Agriculture	1	2	2	2	1	3	1	1	13

Figure 6: Sector Analysis (See

[164] https://www.wsj.com/articles/pg-e-wildfires-and-the-first-climate-change-bankruptcy-11547820006
[165] https://thefuturescentre.org/trend-card/energy-transformation (Accessed 29 March 2019)
[166] https://thefuturescentre.org/trend-card/energy-transformation (Accessed 29 March 2019)
[167] Ibid
[168] https://www.facebook.com/business/news/insights/2019-topics-and-trends-report (Accessed 29 March 2019)
[169] Ibid.
[170] https://thefuturescentre.org/trend-card/future-world-work (Accessed 29 March 2019)
[171] https://thefuturescentre.org/trend-cards/131/healthcare-cure-prevention (Accessed 29 March 2019)
[172] https://thefuturescentre.org/trend-cards/159/hyperconnectivity (Accessed 29 March 2019)

supported to scale up. Taking each sector in turn, we now look at each sector's current state and opportunities to support the social sector.

Education

There are five main segments to the education sector in the UK: early years and childcare provision, primary provision, secondary provision, further education through technical and vocational colleges, and higher education through universities.

There is also alternative provision through pupil referral units, a type of school that caters for children who cannot attend mainstream provision often due to being excluded and needing greater care and support than their school can provide. Research by the BBC has revealed that the number of fixed-term exclusions in the most deprived areas of England has gone up by over 70% in the last four years – four times the rate of the least deprived, which has risen by 15%.[173]

The attainment gap is the difference in performance in exam results between those with different characteristics, such as those who receive free school meals and those who do not, or those with Special Education Needs. Children and young people with low levels of educational attainment are at a much greater risk of becoming NEET (Not in Education, Employment or Training) when they leave statutory education.[174] In almost half (47%) of state-funded mainstream schools, disadvantaged pupils are at least half a grade behind other pupils in each Progress 8 subject.[175]

Between 2016 and 2018, the number of childcare places fell by 251,700 while the number of childcare and early years providers in England reduced by 9.7% from 90,300 to 81,500. Nursery closures have risen 66% since 30 hours free childcare began[176]. Many children arriving at primary school are unable to take part in classroom activities as reported by 83% of school leaders surveyed, and almost nine in 10 respondents saying inadequate school funding was a barrier to improving school readiness[177].

Sector-specific Barriers include:

> Fragmentation of purchasing system, with providers selling more directly to each of the 32,113 schools in the UK[178] and less to central procurement and purchasing teams from the Department for Education or local authorities.

> It is difficult to attribute improvements in long-term outcomes resulting from early years interventions.

> For nursery care in deprived areas where cross-subsidy is less possible, models are dependent on government paying for 30 hours free childcare for working parents. And they don't pay enough to make the models sustainable. "Even those providers who are technically managing to make the 30 hours work are often only able to do so by introducing or increasing additional fees and charges." - Neil Leitch, Chief Executive of Pre-School Learning Alliance[179]

Opportunities include:

> "There is strong evidence that early education can help boost children's outcomes and narrow the gap between disadvantaged children and their peers – but only if it is high quality"[180]

BSC's research identified 15 social organisations working in the education and training sector with turnovers greater than £5m, and a further 13 with turnovers between £1-5m. These include social enterprise early years providers like London Early Years Foundation, teacher-training programmes like Teach First, and academy school providers to healthy school meal providers like Whole School Meals CIC.

Housing / Homebuilding

There is an obvious need in the UK for social enterprises working in the housing and homebuilding sector. This year, 320,000 people were recorded as homeless in Britain, analysis from housing charity Shelter suggests. It is a rise of

[173] https://www.bbc.com/news/av/education-46201155/alternative-provision-schools-we-all-deserve-an-education
[174] https://impetus.org.uk/assets/publications/Report/Make-NEETs-History-Report_ImpetusPEF_January-2014.pdf
[175] https://epi.org.uk/publications-and-research/secondary-school-performance-tables-2018-disadvantage-gap-widens-in-english-and-maths/
[176] https://www.nurseryworld.co.uk/nursery-world/news/1166025/nearly-9-000-childcare-providers-have-closed-since-2016
[177] https://www.nurseryworld.co.uk/nursery-world/news/1162151/shortage-of-funding-barrier-to-school-readiness
[178] https://www.besa.org.uk/key-uk-education-statistics/
[179] https://www.independent.co.uk/news/education/education-news/parents-nursery-fees-30-hours-free-childcare-england-government-funding-mumsnet-a8521421.html (accessed 5 July 2019)
[180] https://www.nurseryworld.co.uk/nursery-world/news/1162151/shortage-of-funding-barrier-to-school-readiness

13,000, or 4%, on last year's figures and equivalent to 36 new people becoming homeless every day.[181]

There are four key elements of the current context of housing and homelessness in the UK: housing demand and supply, homelessness, barriers to accessing housing, and the policy context.

BSC's research identified 64 social organisations working in housing with turnovers greater than £5m, and a further seven with turnovers between £1-5m. These include housing associations, housing trusts and community enterprises like Community Campus '87 Ltd. Community Campus '87 was formed by a group of concerned individuals who were motivated to do something about the growing crisis of youth homelessness on Teesside in the mid 1980's. The primary aim was simply to provide housing with support, to enable homeless young people to gain the skills and experience to get and then keep their own place to live. Employing over 50 staff, apprentices and volunteers it provides affordable housing and support as well as training opportunities across the Teeside area to over 200 people each week.

The housing sector is wildly diverse, ranging from large regulated orgs managing over 100,000 homes (a trend which has accelerated in recent years due to mergers), to those with just a few homes. Their geneses are just as diverse, with some started as community housing organisations from the 1960s, some dating back to Victorian philanthropy, and many created in the 1990s through stock transfers from LAs. There has been a wave of more recently created community land trusts, community and social enterprises like Community Campus and Homes for Good responding to unmet needs.

Sector-specific Barriers include:

> Increasing homelessness
> High capital expenditure required to meet need for new housing stock
> Demographic changes resulting in a mismatch between demand and supply of housing based on family sizes
> An undersupply of Social Rented housing and the growth of the Private Rented Sector has led to threats to housing accessibility, affordability, security and quality for more vulnerable households, having significant implications for health inequalities.
> Insufficiency of revenues to pay the costs of housing and other support costs, particularly with the freeze on Local Housing Allowance and the short-term nature of support contracts;

[181] https://www.bbc.com/news/education-46289259 22 Nov 2018 (Accessed 3 April 2019)

> Availability of, competition for and consequently pricing of land for new development - and the consequent impact on affordability;
> Skills shortages and costs;
> Dependency on private sector developers for new supply via Section 106 orders, resulting in a lack of control over quality, affordability and suitability;
> Ability to innovate product and service to meet changing market needs;
> Risk or perception of mission drift versus competition from commercial house builders
> Ability of social housing providers to articulate their impact properly, and avoid mission drift, particularly when employing cross-subsidy models of investing in market rent or sale properties that subsidise their affordable housing offerings.

Opportunities include:

> Social enterprises may be able to provide housing to households which might otherwise be excluded because they are considered too risky by virtue of having a low income or other issues affecting their ability to sustain a tenancy[182]
> Social enterprises reinvest surpluses in their businesses, possibly enabling them to provide additional services for vulnerable households.[183]
> Larger housing providers accessing institutional equity capital looking for long dated, asset backed returns; Property-backed developments should result in cheaper costs of capital.
> Addressing suitability and affordability in the private rented sector through supporting scaling of social lettings models and affordable build to rent models;
> Designing funding structures that support supported housing providers to build capability and scale, recognising the complexity of their revenue models.
> Larger Housing Associations to become better consumers of scaling social enterprises, given their combined revenues and their supply chains

Retail: Grocery & Food

The UK grocery market accounts for 50p in every £1 of retail sales, and over half of that money is spent in supermarkets[184]. "According to recent UN figures, 8.4 million people in the UK are food insecure"[185]. "A record 1.6m emergency food parcels were given out by the Trussell Trust food bank network last year – more than 500,000 of them to children – as benefit cuts, universal credit delays, and rising poverty fuelled the busiest year in the charity's history." The charity has faced a 73% growth in the use of its food bank services over the past five years, with a growth of 19% just in the last year. [186]

At the same time, childhood obesity is rising. "Obesity is one of the biggest public health threats facing the UK and the biggest human-generated burden on the economy after smoking. Almost one in five children are overweight or obese when they start primary school, rising to one in three when they start secondary school. By 2020, it is estimated half of all children will be overweight or obese. In 2015/2016, 40% of children in England's most deprived areas were overweight or obese, compared to 27% in the most affluent areas."[187]

Finally, the production of food in itself can be very harmful to the natural environment, with continued use of harmful pesticides, herbicides, antibiotics and fossil fuels.

There has been a rise in the number of food-based social enterprises. For example, many Community Shop stores are popping up around the country offering donated surplus food stock from large food retailers at deeply discounted prices. The revenue raised here is used to deliver personal development programmes supporting members to live fulfilling lives, resulting in stronger individuals and more confident communities. Community Shop is a social enterprise run by Company Shop Group, the largest commercial redistributor of surplus food and household products in the UK.

[182] https://static1.squarespace.com/static/543e889fe4b0c26d0d7235e4/t/5899e0cc86e6c0878c74bbd6/1486479572443/HTSE+scoping+report+-+final.pdf (Accessed 3 April 2019)
[183] Ibid.
[184] https://thirdforcenews.org.uk/features/scotlands-social-enterprises-poised-for-a-supermarket-sweep (Accessed 5 July 2019)
[185] https://www.theguardian.com/society/2019/may/19/social-supermarkets-food-poverty-jay-rayner (Accessed 5 July 2019)
[186] https://www.theguardian.com/society/2019/apr/25/food-bank-network-hands-out-record-16m-food-parcels-in-a-year (Accessed 5 July 2019)
[187] https://www.rcpch.ac.uk/key-topics/nutrition-obesity/about-childhood-obesity (Accessed 5 July 2019)

Through a network of six membership-only stores, they purchase surplus food stock and sell them at discounted prices to individuals who work in the food manufacturing supply chain, emergency services or the NHS. Other examples of social enterprises operating in this sector include The People's Supermarket, and That Bread and Butter Thing.

Sector-specific barriers include:

> Rising demand from growing numbers of people falling into destitution and poverty

> At the same time, rising levels of childhood and adult obesity

> Health and safety regulations around redistribution of fresh produce, and shelf life issues

> Competition in the food industry, making it difficult for new entrants who do not have the scale to deliver at affordable price points

Opportunities include:

> Increasing awareness of environmental issues among the public to do with food wastage, and solutions working to combat that.

> Prevalence of food-specific support programmes, like Social Investment Scotland's Social Enterprise Supplier Development Academy

> Emerging business models increasing convenience and availability of fresh, healthy food

> "There are better ways to produce higher quality food that are better for people, the environment and livestock," with lots of innovation happening to disrupt traditional methods of food production and consumption[188]

Example: Eat Balanced & Ugly Drinks

Eat Balanced is a Scottish business that redesigned the pizza to be much healthier without losing or changing the taste. Today, Eat Balanced are one of the UK's leading providers of pizzas for children selling between 30-50,000 pizza portions per week. Eat Balanced sell through schools and family restaurants

Ugly Drinks is a soft drinks company with drinks containing no sugar, calories or sweetener. The company was founded in 2013 in London and is now stocked in Tesco and Sainsbury's

Regional Finance

The most prevalent social purpose regional banks are credit unions. A credit union is a member-owned non-profit institution whose members can borrow from pooled deposits at low interest rates. Like banks, credit unions accept deposits, make loans and provide a wide array of other financial services. They are, however, known for having poor online services, less physical locations and fewer products than traditional banks.

At the end of June 2018, the British credit union sector had:

> Around 292 credit unions across England, Scotland and Wales employing more than 1,700 staff

> 1,342,476 people using credit unions, including 136,491 junior depositors

> Total assets of £1.6 billion

> Total loans of £918 million

> Total deposits of £1.35 billion

> Annual turnover of £115 million (year to June 2018)[189]

[188] https://esmeefairbairn.org.uk/food (Accessed 5 July 2019)

[189] http://www.abcul.org/media-and-research/facts-statistics (Accessed 3rd April 2019)

Other organisations include responsible finance providers. Formerly known as community development finance institutions (CDFIs), they are social enterprises whose mission is to deliver responsible, affordable lending to help individuals, businesses, social enterprises and communities access finance who would otherwise struggle to get funding from mainstream lenders. There are currently around 50 UK responsible finance providers operating in four markets: business, social enterprise, personal and home improvement lending. In 2018, responsible finance providers had lent:

> £85 million to 5,310 businesses, creating and saving 10,370 jobs.

> £138 million to 475 social enterprises, creating and saving 4,060 jobs.

> £26 million in 45,900 loans to individuals; 23,230 of those taking out loans from a responsible finance personal lender had previously borrowed from a high cost lender.

> £5 million to 430 homeowners, bringing homes up to a decent standard and enabling 220 customers to stay in their own homes.

Sector-specific barriers include:

> The industry is underdeveloped and undercapitalised, and therefore incapable of providing community finance to all communities and to all markets across the UK. There is diversity both in type of CDFI, but also within both the CDFIs and Credit Union segments, each facing their own specific barriers. They aren't currently meeting their potential, and could do more to go deeper into the geographies they serve or to move into adjacent areas. In some instances, there isn't a CDFI in the region, which is a challenge.

> Limited data on lending activity and the resultant social impact, although various initiatives are beginning to address this (i.e. Credit Union research by Social Finance, and the Knowledge Centre on the Community Investment Enterprise Facility website)

> Education for digitally excluded individuals expected to use financial services digitally remains a challenge. In addition, financial education and literacy remain a problem for the UK. People need greater support in managing finances, to prevent them falling into problems with debt.

Opportunities include:

> Many CDFIs in the UK are 'sustainable' and don't rely on a steady stream of grant. Some segments are serving clients that are higher risk and therefore grant funding is more appropriate than commercial capital. CDFIs have higher risk tolerance because of their social mission to lend to underserved enterprises/ individuals, the credit unions are conservative on lending because of the rules they have to live up to.

> There is high demand for small scale capital from underserved businesses, often located or serving areas of deprivation

> Embracing technology. Many promising digital solutions will be rolled out further (i.e. video servicing, pre-paid cards, financial management apps, etc.). There is strong potential in Open Banking, which can be used to improve product innovation, encourage budgeting and cut costs.[190] There does need to be a balance between providing a personalised service to people underserved by mainstream lenders, and taking advantage of efficiencies created by using online or lighter-touch relationship/ underwriting processes.

Green & Renewable Energy

Social enterprises operating in the renewable energy sector may be few in number but can be quite large in size. Community Energy England's State of the Sector Report 2018 identified 228 organisations, with over 48,000 members, employing 166 full-time staff and supported by over 1,800 volunteers. With most groups focusing on generating electricity, 168MW of community owned electricity generation was identified, with the vast majority being solar PV followed by wind generation. This generated 202 GWh of electricity in 2017, capable of powering 67,000 homes and reducing CO2 emissions by 71,000 tonnes.

[190] https://www.ukfinance.org.uk/policy-and-guidance/reports-publications/financial-inclusion-digital-age

The infrastructure for the sector is supported by five key community energy developers: Energy4All, Low Carbon Hub, Mongoose Energy, Bath & West Community Energy and Communities for Renewables. Their role is to interface with the community, establish the community vehicle (CIC or Bencom) and its governance, apply for any applicable government subsidies, organise share raises, and often remain involved in the management of projects offering administrative services such as coordinating community benefit funds.

Sector-specific Barriers (according to Community Energy England's State of the Sector 2018):

> Reduction of subsidy support

> Obtaining financing for projects

> Navigating planning processes due to its complexity, lack of transparency and uncertainty of outcome

> Lack of public sector interest in collaborative approaches to solar PV on public buildings

> Local authorities delaying or holding up the development process (e.g. planning permission)

> Lack of viability due to low Feed-in-Tariffs in combination with requirements to establish community benefit fund

> Lack of access to grid due to larger developments within the local area or outbidding

> Lack of access to project management and delivery expertise

Opportunities

> Rapid improvements in technology, such as energy efficiency and energy storage

> New business models for large-scale community energy projects, including long-term energy purchase agreements with non-governmental counterparties, like corporates

> Amalgamation of community energy groups, offering collaboration opportunities

Sport and Recreation

"Sport and recreation means all forms of physical activity which aim at expressing or improving physical fitness and mental well-being."[191] "The sport and recreation sector employs around 371,800 people. This is spread across the public, private and voluntary sectors (SkillsActive, 2011). There are a huge number of volunteers working in sport and recreation. According to Sport England's Active People Survey 4, almost 2 million people in England commit at least one hour a week to volunteering in sport."[192] Despite this, the sector is facing declining funding. Local Authority budgets are still being cut, with sport and leisure budgets down £42m since 2010[193] and culture budgets down £48m in five years[194].

There is a strong and proven link between sports participation and individual level health benefits. Sport England data shows that one in six deaths are caused by inactivity, and that only 56% of adults meet the guidelines of 150 minutes a week of moderate intensity exercise. For over two thirds of those that do undertake this level, sport is part of the activity mix.[195] There is recognition that interventions based on the arts, heritage and sports can be effective ways of tackling specific social problems and of working with vulnerable beneficiaries such as ex-offenders and isolated older people. Programmes that are stimulating and enjoyable help people sustain participation.[196]

Example: Sporting Assets

SPORTING ASSETS

An example of a sport and recreation social enterprise initiative is Sporting Assets, supported by the Access Foundation to create a Sporting Capital fund to support, sustain and grow healthy and resilient communities with sport and physical activity at their heart.

[191] https://warwick.ac.uk/fac/soc/ier/ngrf/lmifuturetrends/sectorscovered/sportandleisure/sectorinfo/industries/ (Accessed 5 July 2019)
[192] https://www.brunel.ac.uk/__data/assets/pdf_file/0019/256321/Sport_and_leisure1.pdf (Accessed 5 July 2019)
[193] https://www.bbc.co.uk/news/uk-england-31624412 (Accessed 5 July 2019)
[194] https://www.artsprofessional.co.uk/news/local-authority-culture-budgets-down-ps48m-5-years (Accessed 5 July 2019)
[195] Source: Sport England health infographics
[196] Big Society Capital: Arts, Heritage, Sport Insight Series

Sector-specific Barriers:

> Lack of acceptance and understanding of social enterprises working in sport[197]

> Difficulty in articulating the impact of sports and recreation interventions

> Many sporting clubs need support becoming more business-savvy and understanding their impact

> Historic reliance on grant-funding by councils and other grantmakers, combined with lumpy income for many community sports and recreation facilities

Opportunities:

> Multiple outcomes possible from sporting and recreation interventions, such as improvements in childhood obesity rates, mental health and other health problems.

> Asset-based interventions make lower-risk investment possible, such as investing in facilities and equipment

> Increased chance of success in crowdfunding and community share offers due to large pool of supporters

> Transfers of sporting and recreation assets to communities from councils (although this poses a risk as well depending on the condition of the assets)

Health & Social Care

One in four charities and one in three social enterprises are involved in the provision of health and social care support. In the current environment, the trend for outsourcing will continue, and with austerity there will be increasing pressure for cost savings and driving efficiency.[198]

The process to spinout has been smoother in health because GPs and other local services are used to managing their affairs. "Primary care is kind of ideal for this. The fact is that general practice runs as a small business. The transition and the understanding of contracting is there."[199]

BSC's research identified 42 social organisations working in health, social care & wellbeing with turnovers greater than £5m, and a further 31 with turnovers between £1-5m. These include many NHS spinouts like CSH Surrey and Bromley Healthcare, to organisations like The Reader in Liverpool who organises Shared Reading groups for looked after children, people in recovery from substance misuse, prisoners, individuals living with dementia, parents, teachers, people with mental and physical health conditions and many more.

Sector-specific barriers include:

> Large contract sizes are difficult for single providers to take on

> Low (sometimes negative) margins on contracts, leading to low reserves

> Short-term nature of contracts, making it difficult to invest, plan and innovate

> Lack of engagement by public sector commissioners

Opportunities include:

> Forming partnerships – both in building consortia for bidding, but also networks to enable sharing of best practice and data to create a more robust evidence-base

> Identifying new income streams and diversifying away from government contracts

> Approaching commissioners in a more joined up way by social enterprises and social investors, particularly in devolution areas where commissioners are seeking solutions and are potentially more open to new models. "Collaboration is key."

[197] https://www.theguardian.com/social-enterprise-network/2013/jan/04/best-bits-social-enterprise-sport (Accessed 5 July 2019)

[198] http://e3m.org.uk/capital-for-growth-health-and-care/

[199] https://www.theguardian.com/healthcare-network/2014/apr/30/health-sector-spin-outs-ownership (Accessed 5 July 2019)

Conclusions

There are a number of sectors where social enterprises should be able to thrive and grow, based on the sector's economics as well as competitive advantages specific to social enterprises given their mission alignment to each sector.

There is also a parallel yet significant opportunity for increasing social impact by supporting and growing *commercial businesses* that provide a superior employment offer in sectors with large amounts of lower skill employment in deprived areas. This would include businesses operating in areas like care homes, distribution, hospitality, retail, etc. If companies in those sectors paid the living wage, offered training, and offered fair and secure contracts, that would go a long way to fighting poverty and inequality in marginal labour markets.

The top priority sectors for social enterprises are:

> Education

> Housing / Homebuilding

> Retail: Grocery & Food

> Regional banks / finance

> Green & Renewable Energy

> Recreation

> Healthcare

Housing associations, universities, hospices, and academy school chains are some examples of large-scale social enterprises that have thrived in these sectors. These have succeeded due to government subsidies whether capital or revenue, which have been provided because governments have seen them as vital to society and the economy.

Each sector has a differing level of existing social enterprise activity - some great in number, some great in scale. **The top 5-10 ready to scale social enterprises from these priority sectors should be identified every year and supported as much as possible to scale up**.

The Vision

It is entirely conceivable to see hundreds if not thousands of social enterprises growing to a scale where their economic and social impact positively changes the fabric of our society. A compelling and achievable vision for the near future is to see **one hundred more social enterprises reach scale across a range of priority sectors in the next five years.**

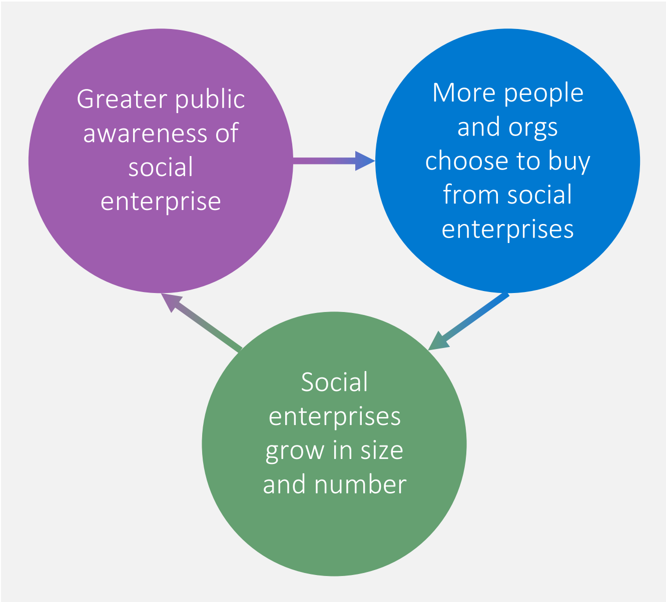
Social enterprises have many advantages in getting to scale over their commercial counterparts, such as attracting passionate talent, but also face additional and unique barriers. To achieve the vision, shifting from a focus on entrepreneurship to scaling what works, and backing our winners properly, is essential. In practice this means supporting scaleups to address the barriers that affect both them and commercial businesses alike.

Specifically, eight areas of support are critical to see this vision through to fruition:

1. Build, or attract, scaling skills and experience in scaleup management teams (including financial, operational and impact management)
2. Find and retain great talent, through developing more effective recruitment practices and stronger talent development programmes, offering better sector wages without stigma, and seeing macro policy changes make it easier to recruit globally[200]
3. Expand to new markets, not only defined geographically but also reducing reliance on one or two large contracts, to a more diverse and global customer base
4. Strengthen organisation infrastructure as standard (e.g. implementing HR, CRM and finance systems, policies and procedures that can handle higher volumes of sales)
5. Ensure high quality products and services, and a skilled practice in marketing and branding, to help change market perceptions of social enterprise
6. Easily access sector-specific support to develop scalable business models, attract investors willing to pay for impact in a sector, and share resources like talent and procurement networks
7. Maintain good mental health in the entrepreneur and management team, and healthy and effective workplace cultures
8. Share and learn from successful scaling peers across sectors to help overcome challenges

A key part of the vision is building a stronger movement around social enterprises, making it clear who they are, what they do, and how they benefit society while delivering high quality, useful products and services. In this way, we can create a virtuous circle of growing numbers of socially-minded businesses, all procuring from each other, and thus growing in scale themselves.

[200] ScaleUp Institute: Annual Scaleup Review 2018



Case study: B-Corporations

B-Corps are a community of leaders, driving a global movement of people using business as a force for good. These are businesses who self-identify as having a purpose beyond profit, and need to score at 80 out of 200 questions on a rigorous scoring system covering Governance, Workers, Community and Environment to prove it. There are 170 certified B-Corps in the UK, including brands like Waitrose & John Lewis Partnership, The Big Issue, Divine Chocolate, Pukka, Bulb Energy, JoJo Maman Bebe, Toast Ale, Propercorn, Abel & Cole, Brewgooder, Innocent Smoothies, Ella's Kitchen, Cafe Direct, among others.

By being certified as a B-Corp, they join a network of like-minded businesses and business leaders, and are supported to procure from each other and support each other's growth. They are also growing fast. Average year-on-year growth across the 150 UK B Corps was 14% in 2017 compared with 0.5% growth in GDP by the start of 2018.

A third (35%) of certified UK companies said they had attracted new audiences since joining up, while almost half (48%) found that prospective staff had been attracted to the business specifically because it was a B-Corp.

Lesson: Purpose is beginning to pay off at scale. Being part of a community of like-minded businesses brings many benefits, including faster growth and a more engaged workforce.

Some ideas for ways to deliver the eight identified areas of support include:

> **Launch a permanent (i.e. not programmatic or time limited) social enterprise scale readiness programme that addresses all eight critical support areas, with a focus on barriers unique to social enterprises.** This might engage a cohort of ten social enterprises per year, focused on a different priority sector each year. In parallel, cohort businesses could be connected to the most relevant ScaleUp Institute endorsed programmes to reduce cost and avoid duplication of effort. Depending on their needs, each enterprise would receive between £50k - £100k of grant funding per year for up to two years to cover purchasing new systems, consulting fees, research and implementation costs. Assuming programme costs of £200k per year[201], a total recurring annual budget for this programme would be £1.7m. It could include the following, tailored to each business' needs:
  > Impact strategy, management, measurement and reporting support
  > Advice and training for enterprises to set scaling strategies for their impact models, including innovation capability development
  > Recruitment support for sector-specific skills, including systems thinking and impact
  > Support to select, purchase and implement bespoke CRM, finance, impact management and other systems, using programme grant funding
  > Codifying the business' operations into manuals, policies, processes and procedures, and implementing quality controls and sales metrics
  > Support negotiating legal agreements, partnerships, and supply chain contracts[202]
  > Support developing a strong brand, with deep customer understanding and insight, and a great marketing function
  > Support developing a shared understanding of cultural and consumer preferences
  > Ensuring the financial position of the business is secure and well understood
  > Access to expert mentors to provide key advice, connections and customers, particularly around expansion to new markets - likely through partnerships with other scale support programmes

Over ten years, this programme would see one hundred social enterprises operating at scale (>£10m turnover) and creating diverse, measurable, tangible impact in the UK for a total cost of £17m.

> Create a scaling talent pool for account managers, and candidates with proven scaling experience (addresses support area one and two). It could identify and carefully select excellent people with track records in scaling businesses who are interested in working in social enterprises. This might also allow progression between social enterprises for scaling experts.

Large scaleup investor BGF's Talent Network is one of the largest groups of board-level non-executives in the UK. BGF has a team dedicated to developing the Network, who match-make the most relevant non-executive directors, advisors, and experienced interim managers into the companies it backs.

> Create networks of scaling social enterprises so they can share and learn from successful peers (addresses support areas five, six, seven and eight). This could range from arranging informal networks, to setting up new formalised networks, to using existing networks like B-Corps or E3M, taking advantage of existing brands. A social enterprise scalers peer-to-peer network could be created within the existing B-Corps infrastructure. This would provide leadership development opportunities, as well as a network of like-minded businesses who could procure from each other, refer others to potential clients, etc.

> In addition, local networks could be created to help scalers develop local supply chains, building and strengthening local economies.

[201] Programme costs assumed to cover a managing director post at £90k (£110k including on costs), one programme directors at £60k (£75k including on costs), and £15k allocation for administration and office costs, assuming the programme could be hosted at a partner organisation's premises. The resulting caseload of each employee would be supporting no more than five businesses to scale per year. All consultancy and research costs would come out of each business' grant funding.

[202] https://ssir.org/articles/entry/to_impact_millions_the_social_sector_needs_to_scale_scaling_up (Greg Coussa, Jan 24 2019)

This helps create genuine impact at scale through all areas of a business' operations.

E3M is an initiative that promotes social innovation in the way public services are run. In particular, it supports the growth, scale and impact of over 30 of the UK's top social enterprises that trade in public service markets, providing them legal, financial and other expert support from partners.

> Partner with organisations like Mind, and other ScaleUp Institute endorsed leadership programmes to provide coaching and mental health support for management team members.

Capital to Support this Vision

Successful social scaleups have the potential to create more public benefit than commercial ones, given their dual missions of delivering both profit and impact. An important way to support social scaleups to thrive is attracting diverse investors with differing risk/return expectations to make more capital available on fair terms.

Access to capital is commonly cited as a barrier to scaling up. How can we best design capital to support social scaleups? Let's start with the basics of investment to understand what's possible.

Investment 101

An investment is made when a person or entity with money agrees to give it or lend it to a business for a certain period of time, in exchange for the chance of a return – getting back their money plus some. That chance is called risk by investors. To increase the capital available for social scaleups we need to consider what will attract more investors.

Equity

Where there is a high risk of investors not getting their money back, they will only invest where there is a possibility of a high return. This is usually done through an equity investment, where in exchange for its money the investor takes a share of ownership of the business and only ever sees their money again when that business is sold, or another investor buys their share.

By "high return", investors usually mean a return high enough to compensate them for their potential losses as well as provide them with a profit. In practice, this means they may be investing across many businesses at a similar level of high risk, where many are likely to fail and return much less money than the investors' original stake. The ones that do survive need to pay back the investors enough money to cover the losses they sustained on the other businesses and compensate them with some profit to make the whole thing worth the trouble.

The earlier a business is in its stage of life, the riskier it is. The younger it is, the less it has had the time to prove that people actually want to buy what it is selling, that it can drum up demand for that product or service, and that it can operationally respond to customer orders and deliver high quality, on time. The riskiest life stage of a business is start-up, before it has any revenue, and then before it has made a profit. Once the difficult job of proving the concept is done, and as a business scales, it becomes more reliant on operational excellence. When the market opportunity has been proven, a business will be considered less risky to its investors.

Debt

On the other hand, an investor can choose to take a much lower risk, and therefore a higher chance of getting their money back, by agreeing to loan a business money. The investor does not take an ownership stake in the business, and the business pays the investor's money back over time through regular instalments. The business also agrees to pay the investor her return through a fixed interest rate, which is also paid over regular instalments. The business will be assessed based on their ability to keep up their payments, or their incoming cashflow minus their other outgoings. The business will need to be comfortable committing to that level of regular repayment over the life, or term, of the loan.

Debt can be secured (usually on property or other assets) or unsecured. If it is secured, then if things go wrong the investor can sell the thing the loan was secured against to recover their money. A mortgage is a good example of a secured loan. Big banks charge anywhere from 2-4% per annum for a standard mortgage, but their loans are backed by a property (the house) meaning there is little risk to the investor not to recover their original loan. If the homeowner stops paying their monthly dues, the bank has the right to step in, sell the house and get mostly all of its money back. That's why mortgages are the one of the cheapest forms of finance on the market – the risk to the investor is very low.

Quasi-Equity

Quasi-equity exists because some businesses' legal form means they cannot easily accept equity investment, yet they still need money to grow and the capital required poses a higher risk than debt providers will take. The most common corporate form that can take on equity investment are Companies Limited by Shares (CLS). Social enterprises can be legally registered as CLSs, but in the UK they can also be registered as: Community Interest Companies (CICs, limited by either shares or guarantee); Registered Charities that are Companies Limited by Guarantee (CLG) or in rare instances, Companies Limited by Shares (CLS); Industrial and Provident Societies that exist either for the benefit of the community (BenComs) or for the benefit of their members (Co-ops); Charitable Incorporated Organisations (CIO); or Charitable Trusts. These entities either may not have shares to sell (e.g. CLG), or they are often regulated such that private gain and profit is capped or forbidden. This makes it harder for them to attract investors.

Quasi-equity has been used to overcome the barrier of not being able to take equity investment, and is a hybrid of debt and equity. Investors take equity-like higher risk, without having an ownership slice of the business, and get their money back through regular debt-like repayments at an agreed fixed interest rate usually based on a company's revenue or profit. The debt is often unsecured, and is generally unrecoverable if things go wrong. To compensate for the high risk the investor is taking, this interest rate will be higher - much higher than say a mortgage.

Investor Needs, or Cost of Capital

The two key components, therefore, of any investment decision from the investor's point of view are risk (i.e. "what are the chances I will get my money back, and then some?") and potential return. *Social* investors also consider the social impact of their investments – how will making this investment deliver measurable benefit (some social investors also care that the resulting benefit wouldn't have happened otherwise) as well as provide a fair financial return?

This leads to the question of what is a fair return. The way the market currently works, this is dictated by market forces - supply and demand. In fact, the only return available is the rate investors will accept to compensate them for the risk they are taking in giving a business their money ("risk-adjusted return") - on terms acceptable to that business. From the expected return, funders need to pay their own costs, both of their own staff and overheads but also the cost of their capital, pay for bad investments, and make a profit. This adds up to the total cost of finance to the investee.

Investee (Social Enterprise's) Needs

From the investee's perspective, they are looking to find a trusted partner who, if given a slice of ownership of the business they have put years of hard work into, won't take control of it, grow it in unsustainable ways, and sacrifice its social mission for more profit. They are also looking for a good deal. They want to find the cheapest possible debt to be able to put more of their hard-earned income towards serving their beneficiaries rather than their investors' pockets.

Additionally, social enterprises need to be careful when taking on too much debt to grow, particularly those who aren't CLSs. With too much debt on a company's Balance Sheet, a business has lots of regular payment commitments to meet, which can put pressure on their cashflow. Often, they raise further debt to repay the first lot of debt - kind of like getting a new credit card to consolidate old ones. When they then want to raise money to grow, a whole lot of that money is spent repaying old investors, and not investing into the business itself. This situation can become very precarious for the business.

Market Forces of Supply and Demand

In general, capital (i.e. money) will become available to investees if it is likely to provide the *social* investor with the fair risk-adjusted financial return she seeks, as well as demonstrable impact. Exceptions to this include where there is a stakeholder of the investee who is willing and able to provide growth capital on different terms - e.g. friends and family or local authorities. Deals will only become available to investors if there is a trusted relationship, and fair terms for the potential investee.

Across different markets, advantage can be skewed either towards investors or towards businesses depending on supply and demand. Investors can be advantaged if there is a large demand for their capital, allowing them to pick and choose from investees: there are more opportunities to invest than there is capital. In other markets, businesses have the advantage and can choose investors among many. Some very good businesses get lots of interest and multiple offers from investors, and the balance of power shifts in their favour.

Some businesses that struggle to raise institutional investment (i.e. from other companies like venture capitalists), benefit from family and friends who invest, or from government tax breaks (like VCT, EIS, SEIS and SITR) that incentivise investors to invest when the risk-adjusted return might not be adequate on its own.

Investees need to think carefully about their paths to growth, and how fast they want to scale. As mentioned earlier, other paths to scale exist, like organic growth that might not involve external investors, but reinvesting surpluses and growing slowly. It is worth considering what the price is of delivering a higher return or paying a higher interest rate in terms of both cashflow and ability to have more impact more quickly. If a business model and cashflow can afford it, is it worth taking on growth capital to be able to scaleup and reach five or ten times more beneficiaries much quicker?

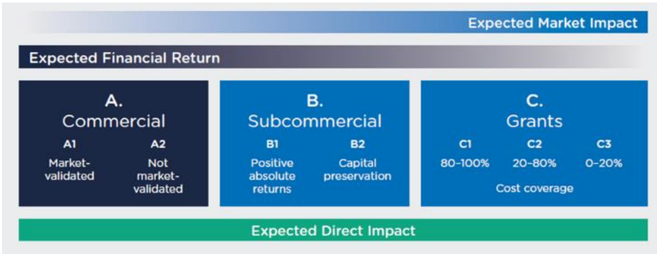
Catalytic Capital

Sometimes a social enterprise cannot produce or afford the returns demanded by available investors, but they might be very likely to produce a positive return, or at least return initial capital (capital preservation), and are creating important, measurable impact. It is likely these businesses will never be able to access market-rate investment because the risk they pose is too great, and their return potential is not enough to attract many investors.

Catalytic capital, also called patient, concessionary, or flexible capital, is one solution. There are investors who are not seeking a market-rate return - that is, the rate of return where supply of capital meets demand. Their interests lie in supporting impactful interventions in areas that are of importance to them, making sure they scale and reach as many people who need them as possible.

Omidyar Network in their useful paper "Across the Returns Continuum" suggest the right question to ask is "under what conditions should an investor accept a risk-adjusted below-market return in exchange for an opportunity to achieve social impact?" Omidyar believe there to be "a broad range of viable investment profiles, some of which involve a trade-off between social return and financial impact, and many of which do not."[203] Omidyar sets out the following framework to help impact investors classify the investments they make along this spectrum.

Figure 7: Omidyar Network's Spectrum of Capital Framework



In this model, **Segment A** businesses have the potential to produce market-rate returns, and have either raised commercial capital (A1), or not (A2). In segment A2, the potential for market-rate returns exists but the business may be selling to low income consumers that commercial funders might not consider profitable, or may be operating

[203] https://www.omidyar.com/spotlight/how-do-we-invest-across-returns-continuum (Accessed 18 April 2019)

in markets with a small number and size of investor.

Segment B businesses will never deliver market-rate returns. They do, however, have the potential to either deliver positive returns (B1), or at least return the investor's initial stake (B2).

Finally, **Segment C** businesses will never return even an investor's original stake, and require grant funding to grow their work. They exist on a spectrum from those that develop revenue models over time that cover 80-100% of their costs (C1), to never being able to cover more than 20% of their costs (C3).

Crucially, across all segments direct impact (i.e. the impact of the business itself) is imperative. And as financial return potential decreases, market-level impact, or "systems change" is of increasing importance to Omidyar when making investment decisions. We will use this framework to explore possible solutions later on.

Exit Considerations

As mentioned before, equity investors only receive their money back when the business they've invested in is sold, or another investor buys their stake. Often investors have to return their money to their own investors within a specified time frame – typically ten years. This means that they must "exit" their investments, or sell their stake, within that ten-year period. This is restrictive for many social enterprises who may take a longer time to grow, and who may not want to sell their business within the period.

Case study: Zebras Unite

Zebras Unite is a movement calling for a more ethical and inclusive venture capital market. It is an online community of more than 1,500 values-driven entrepreneurs, with 40 chapters across six continents. The founders had trouble raising finance: "social impact investors don't work in our space, and venture capitalists won't fund companies that can't promise 10x returns. We'd created... companies with purpose and then discovered this type of company is basically unfundable."[204]

The movement launched following a Medium post called 'Zebras fix what Unicorns Break' explaining:

> "To state the obvious: unlike unicorns, zebras are real.

> "Zebra companies are both black and white: they are profitable and improve society. They won't sacrifice one for the other.

> "Zebras are also mutualistic: by banding together in groups, they protect and preserve one another. Their individual input results in stronger collective output.

> "Zebra companies are built with peerless stamina and capital efficiency, as long as conditions allow them to survive."

This raises some big questions: how can investors support businesses who don't want to sell within ten years, or go public? And how can investors make their return if the winners aren't paying back enough to cover the losers? The movement's answer to the first is through ongoing proportionate profit sharing rather than relying on an exit event. This would require investors not to have a specific time horizon within which they need to close their funds and return capital to their own investors. These businesses may offer a lower prospect of return, but if they are lower risk to invest in, they should be investable. Investors should be able to design funds that work by taking lower risk in exchange for lower return.

[204] Photo: https://medium.com/@sexandstartups/zebras-lets-get-in-formation-fdcbc72fec4a

Financing Social Scaleups

To achieve this paper's vision, finance is required. For social enterprises to grow, they need capital. Risk capital allows social enterprises to take the risk of scaling up their operations ahead of being able to take on or tendering for large contracts. Just like in the private sector, that capital is used to invest in teams, systems, strategies, raw materials, and additionally, impact measurement and management.

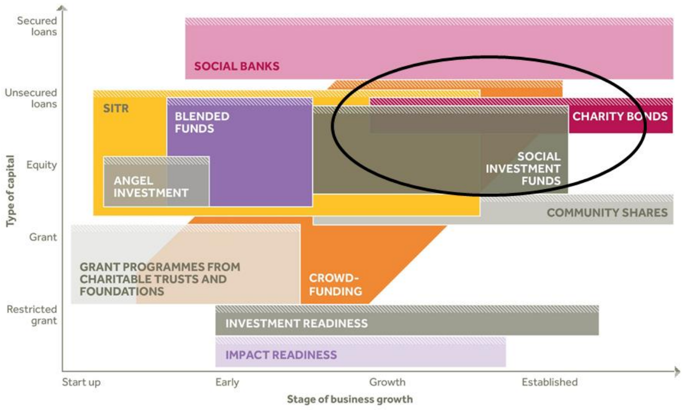
As we've seen in previous sections, the majority of UK SMEs do not take on investment. As previously noted, only 9% of SMEs sought external finance in 2017, with equity finance used by only 2% of SME employers according to the LSBS. Of those that do, there are well-trod paths in accessing finance. Nesta's report Paths to Scale (2019) looks at 26 European entrepreneurs and identifies eight sources of finance these commercial scaleups used:

1. Bootstrapping, or self-funding (Organic Growth)
2. Crowdfunding, from individuals on online platforms
3. Angel Investment, from individuals investing their own money
4. Venture Capital, from institutional investors or larger corporations
5. Initial Coin Offering (ICO), from public investors using cryptocurrencies
6. Corporate Acquisition, through acquisitions by corporations
7. Initial Public Offering (IPO), by selling shares to public investors on the stock market
8. Private placement, from a small group of selected investors through a private offering

Of these sources, most are available and being used currently by social enterprises, as reported by SEUK (grants, loans, and "equity" which we take to mean Angel and Venture Capital). The few which aren't as prevalent yet, but still have some examples, are ICO, Corporate Acquisition, IPO and Private placement – financing sources usually reserved for quite large businesses. Generally, if a business is considered good enough (i.e. potential to deliver risk-adjusted returns), it will have its choice of investor.

In addition to the sources identified by the Nesta report, there are a number of routes that have been used by social scale ups for some time. The capital need to scaleup up social enterprises is presented on the picture below – a need for appropriate equity or unsecured loans at later stages of business growth. As can be seen, there are a few existing options for capital, including crowdfunding (e.g. Eden Project), charity bonds (e.g. Welsh Water and GLL) and some social investment funds like the Bridges Evergreen Fund.

Figure 8: Social Investment capital available to social enterprises in the UK



Secured finance from commercial or social banks can be an important low cost option where the risk of the business model and balance sheet allows it. Again depending on the models and stakeholder relationships other important alternative sources of scale-up capital can include local authority loans (e.g. Robin Hood Energy) and leasing (e.g. HCT)[205].

[205] BSC Social Investment Market Compendium 2014

Financing Start-ups vs Scaleups

BSC research shows the bleak picture that early-stage venture capital investing paints, deriving the majority of returns from a very small proportion of overall portfolio.

Table 8: Venture returns dispersion and exit values across multiple funds in BSC's portfolio and various sector reports

Source	Fund A	Fund C	Angel returns report	Correlation Ventures Report	European VC Landscape	Nesta Angels Report	ACEF Project	Fund D
Year	2017	2017	2016	2004 - 2013	2017	2009	2009	2014
Stage	Venture	Angel	Angel	Venture	Venture	Angel	Angel	Venture
0	87%	78%	70%	65%	57%	41%	35%	20%
<1x	0%	0%			13%	15%	17%	16%
1x to 5x	9%	3%	18%	25%	25%	35%	34%	64%
5x to 10x	4%	7%	6%	0%	4%	3%	7%	0%
10x to 30x	0%	10%	4%	3%		5%	3%	0%
>30x	0%	2%	2%	2%		1%	4%	0%

Investing in scaleups, also known as providing growth equity, should be less risky than investing in start-ups as by the time they are scaling up they will have proven their product-market fit, and it becomes more about execution than proving the concept. Cambridge Associates find that exact conclusion.

> "Venture capital is reliant on a small subset of investments (8% of capital) for half of the value it delivers. In contrast, growth equity capital generated 28% of its total value from investments with MOICs greater than 5.0x and buyouts generated just 18%. Both growth equity (31%) and buyouts (35%) have a larger percentage of capital invested in deals generating a narrower band of outcomes (between 2x and 5x) than venture capital (18%)"[206]

The data from this quote can be understood graphically in Figure nine.

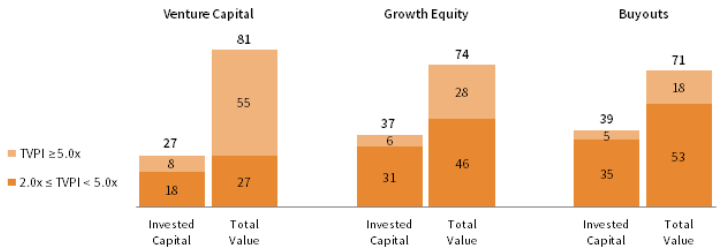


Figure 9: Investment-level Returns Dispersion as of June 30, 2018 (Percent (%))

Cambridge Associates also find that the more annual revenue growth a company can deliver and sustain, the higher returns they actually deliver. So investing successfully in scaleups becomes all about creating and sustaining growth.

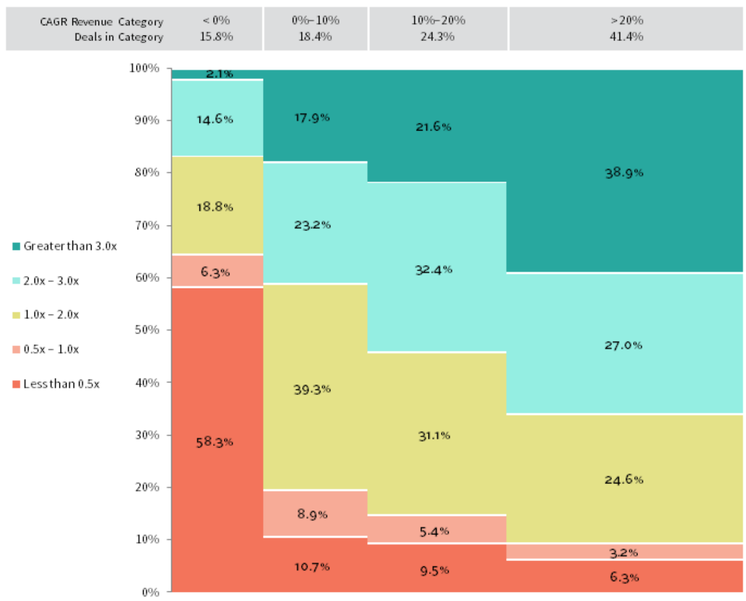


Figure 10: US Growth Equity: Realized Multiple of Invested Capital (MOIC) By Revenue Growth as of December 31, 2017

The ultimate goal is to ensure that good social enterprises achieving significant social impact with potential to scaleup can access the finance they need to grow. The ability to access commercial capital will greatly increase their chance of success, given the scale of capital they will likely need and the scale of commercial capital that exists compared to social investment or investors seeking concessionary returns.

Framework

Different businesses face different challenges, and will therefore require different solutions. Using the Returns Continuum framework, five segments of social enterprise are analysed in their current ability to access finance in Table nine below.

[206] https://www.cambridgeassociates.com/research/growth-equity-turns-out-its-all-about-the-growth/

Table 9: Ability to Access Finance by Spectrum of Capital segment

Segment	Description	Access to Finance
A1	Potential to deliver market-rate return, and already has market-rate investors	Market operating properly: likely significant access to potential investors
A2	Potential to deliver market-rate return, and does NOT have equity market investors	Market-rate equity investors could invest, but have not yet due to lack of track record, and information asymmetry: impact of social model on risk-return potential.
B1	Potential to deliver positive but *less* than risk-adjusted market-rate returns	Market rate equity investors will not invest; requires catalytic capital or other intervention to access capital. Depending on model, debt-like market rate capital may be available such as bonds and leasing.
B2	Potential to return only initial capital	Market rate equity investors will not invest; requires catalytic capital or other intervention to access capital. Unlikely debt investors will be available.
C	Not able to return initial stake	Grant funding required

Categorisation by segment does not depend on a social enterprise's legal form – only on the ability of its business model to generate profit, and what it chooses to do with those profits. All the common forms of regulated entities have restrictions on what they can do with profits, but all are legally permitted to pay a cost of capital such as paying interest on a loan.

As mentioned, only social enterprises legally structured as CLSs have significant flexibility on raising equity, which is how commercial ventures access risk capital. Regulated social enterprises who cannot take on equity investment need other forms of risk capital, like quasi-equity. These businesses have similar needs to help them address the barriers to scale, but will require different approaches to finance.

Segment A1 is excluded from this analysis given the already well-functioning market, while segment C is excluded due to indefinite reliance on grant funding. In each remaining segment, different approaches are required to ensure capital is made available to the best social enterprises.

Case study: Welsh Water

Segment: A1

Welsh Water is the sixth largest of the ten regulated water and sewerage companies in England and Wales with a turnover of £757 million. Responsible for providing over three million people with a continuous, high quality supply of drinking water and for taking away, treating and properly disposing of the wastewater that is produced, it is fully committed to delivering best quality service at least possible cost. It intends that every customer should receive a safe and reliable service that meets all their expectations, at a price that is affordable and below that charged by other equivalent UK water companies.

Since 2001, it has been owned, financed and managed by Glas Cymru. Unique in the water and sewerage sector, Glas Cymru is a company limited by guarantee and as such has no shareholders. Any financial surpluses made are retained for the benefit of Welsh Water's customers.

Glas Cymru was created by Nigel Annett and Chris Jones in 2000, with the support of its first Chairman Lord Burns, for the sole purpose of acquiring and then managing Dŵr Cymru Welsh Water, the water and sewerage service provider in most of Wales and some adjoining parts of England. After a process that took around 18 months, Glas Cymru successfully acquired Welsh Water from Western Power Distribution (a US owned electricity network company) in May 2001, financed by a £1.9 billion bond issue (thought to be the largest ever, non-government backed, Sterling corporate bond issue).

Successes of the group to date include:

> some £3 billion invested to improve drinking water quality, environmental protection and customer service – at no cost to the taxpayer

> financial gearing reduced from 93% to around 65% are reflected in improved credit ratings (A/A3/A) which are the strongest in the UK water sector

> around £180 million returned to customers in the form of 'customer dividends' and over £10 million of support for disadvantaged customer groups via social tariffs and an assistance fund

> lower average customer bills in real terms than in 2000, in part due to the best record in the sector in cost reduction and improved efficiency.[207]

Segment A2

Problem: For social ventures capable of achieving risk-adjusted market rate financial returns alongside impact, there is often a lack of information, especially on track record and establishing product/market fit, leading to a misunderstanding of the risk and return profile by commercial investors. The time horizon for investors realising their returns might also be very long due to the very nature of these businesses to attract commercial capital. The business and impact models of this segment have not yet been validated to such an extent that commercial capital would readily invest. Once models are validated and commercial capital is invested, these businesses shift up into segment A1. Social investors, who may better understand the

[207] https://www.dwrcymru.com/en/Company-Information/Glas-Cymru.aspx (Accessed 14 March 2019)

interplay between impact models and profitability, can and should invest in a collection of these businesses if they believe the business models will deliver market-rate returns.

Some examples include social housing and community energy projects. In these examples, the businesses themselves might be quite small, but require a large amount of project finance capital. Once projects are built, they are often capable of delivering market-rate returns and are able to refinance large portions of their investment capital to banks, pension funds and other institutions. Asset-backed debt is easier for social investors to provide, enabling these businesses to prove their models. Other examples include charity bonds, as well as investing equity directly into growing enterprises who are themselves addressing specific social issues such as financial inclusion, childhood obesity and ageing.

Regulated SEs: For social scaleups with legal forms that restrict their ability to take on equity, quasi-equity should be available. The possibility of risk-adjusted market rate returns means there should be many potential investors. Funds sometimes struggle to deploy quasi-equity due to both an inability to find regulated social enterprises delivering market-rate returns, as well as a reluctance or inability by the businesses to pay the level of return required to compensate the investor for the risk taken. This nudges those businesses into segment B.

Potential Solutions: The goal of getting capital to this segment is to support the profitable creation of impact, and prove their models. By validating models quickly, commercial capital can be attracted in, pushing some businesses up into segment A1. Others will need longer to prove their models. To get investment to these models, either:

1. impact investors need to be convinced their capital will have both a big impact and sizeable returns to compensate them for taking a higher risk on a not-yet-validated model;
2. other mechanisms such as guarantees and first-mover or catalytic capital need to be used to de-risk investments by taking a junior position encouraging other capital to flow;
3. scaleups themselves are de-risked to increase their chance of success;
4. confidence to invest is developed through co-investment; or
5. longer investment time horizons are employed, such as those called for in the Government's Patient Capital Review.

Impact Investors

Impact investors are a distinct group of investors who will take uncertainty for the promise of impact alongside risk-adjusted returns. Impact investors can and do invest in these business, recognising the impact potential, as well as the potential for a market-rate return. Existing funds that provide this kind of capital in the UK include SASC's Third Sector Investment Fund, Ascension Ventures' Fair by Design Fund, and Bridges' Evergreen Fund.

There is currently not enough capital in the UK social investment market to fund all of the social scaleups who fit this category. Given the amount of capital scaleups need to grow and thrive, existing funds need to raise much more capital to meet this need. This, alongside quantitative research to determine the exact size and nature of the capital need, would help ensure A2 businesses have the best chance at reaching scale.

Guarantees

Other interventions like investor guarantees can be used to crowd in more capital. There are two main ways to guarantee investor returns are to:

1. provide a guarantee such that in the case an investment goes wrong, the investor receives an agreed proportion of their principal, and/or interest (See EIF case study below)
2. provide tax reliefs and breaks to investors. This effectively guarantees a set portion of their investment through corresponding reductions in tax liabilities, which incentivises investment into businesses where the risk-adjusted return might not be enough on its own.

As segment A2 models have the potential to deliver market-rate returns, guarantees could be employed to reduce the risk to investors and encourage them to invest before a model has been fully validated. Guarantees are already used to good success in the EU, through the European Investment Fund.

Case study: European Investment Fund (EIF)

EUROPEAN INVESTMENT FUND

The European Investment Fund (EIF) supports Europe's SMEs by improving their access to finance through a wide range of financial instruments deployed by intermediaries. EIF designs, promotes and implements equity and debt financial instruments that specifically target SMEs.

Launched in 2015, the €196m[208] EaSI Social Entrepreneurship Guarantee, managed by the EIF on behalf of the European Union, has a key objective of increasing access to finance to social enterprises. It provides capped guarantees and counter-guarantees to intermediaries who lend to social enterprises. The guarantee covers up to 80% of losses incurred by intermediaries across their social enterprise portfolios up to a capped amount of up to 30% of their total portfolio volume. For example, for a £10m fund providing debt products to social enterprises, £2.4m in losses would be guaranteed (80% of £300k). A variety of debt products are eligible including loans, mezzanine loans, subordinated debt, leases and profit-sharing loans. The guarantee is expected to support 1,350 social enterprises in Europe over its five-year life[209].

In addition to the EaSI Guarantee, EIF run the €150m EFSI Equity Programme. EFSI Equity provides equity investments to or alongside impact investors focusing on the areas of early stage, growth stage and expansion financing. The programme will invest alongside three types of investor: i) incubators and accelerators, ii) business angels or angel funds, and iii) intermediaries working on Payment-by-Results or Social Impact Bonds.

Tax reliefs are also widely used in the UK through Venture Capital Trusts (VCTs), Enterprise Investment Scheme (EIS), Seed Enterprise Investment Scheme (SEIS), and Social Investment Tax Relief (SITR). These tax reliefs guarantee an investor will receive a certain percentage of their investment capital, ranging from 30%-50%, back in the form of a reduced income tax bill. They also often reduce, eliminate or defer other tax due, such as capital gains tax or income tax payable on dividends received.

Social Investment Tax Relief (SITR) was launched in 2014 and, similarly to the other venture capital tax reliefs, gives investors in regulated social enterprises an income tax reduction worth 30% of the value of their investment. Unfortunately SITR has had limited take up thus far. As of May 2018, 50 social enterprises had used the relief over its lifetime, raising a total of £5.1m in investment[210]. Updating some of the restrictions around SITR would help increase its use, as well as help certain segments of scaling social enterprise to raise finance. One recommendation would be to rethink the restrictions on lending organisations using the tax relief, given the number of social enterprises working on financial inclusion by providing ethical loans to people in need and struggling to scale.

First-mover or Catalytic Capital

Interested parties, like government and mission-aligned foundations who have vested interests in seeing the impact of these businesses scaled, might choose to take riskier positions to encourage even more capital to flow. There is a role for those institutions to take junior positions in funds that are struggling to raise the capital they need to support more of these businesses to scale. A relatively small amount that takes a lot of the risk can catalyse a much greater amount of investment to flow. Given the nature of this segment, there is high probability of achieving a good return, as well as catalysing the scale of investment required.

[208] https://www.european-microfinance.org/news/boost-eu100-million-microfinance-and-social-enterprises-europe
[209] http://www.eif.org/news_centre/publications/EIF_Working_Paper_2017_39.htm
[210] https://www.gov.uk/government/statistics/enterprise-investment-scheme-seed-enterprise-investment-scheme-and-social-investment-tax-relief-statistics-may-2018

Example: Bridges Fund Management

Bridges Fund Management's first fund, the Community Development Venture (CDV) Fund I, raised £20 million of private sector investment in 2002 and was backed with matching investment from the Department of Trade and Industry. Its second CDV fund went on to raise £75m in 2007, all from private sources[211]. Seventeen years later and Bridges has now raised over £900m to invest in solutions to pressing social and environmental challenges[212]. The UK Government's initial £20m investment into an unproven fund manager and concept catalysed over 45 times more private capital to solve social problems.

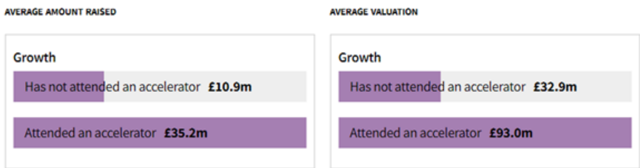
De-Risking Social Scaleups

This paper has explored all the barriers that both commercial and social scaleups face. De-risking social scaleups involves systematically addressing these. Four components together can de-risk social scaleups:

1. Strong infrastructure in terms of team, systems, sales processes, and controls
2. Shared talent pools & stronger people strategies to develop scaling skills
3. Building a stronger social enterprise movement
4. Market side initiatives

Scale readiness is necessary to help social scaleups address the many barriers they face. A scale readiness accelerator/programme, as recommended earlier, would not only help each venture improve and get ready operationally for scale, it would also act to de-risk the venture at a critical stage in its growth. According to Beauhurst research, accelerated companies raise 44% more and at a 75% higher valuation[213].

Figure 11: Amount of capital raised by ventures having been through accelerator programmes or not (Beauhurst)



The largest barrier common to both commercial and social scaleups is access to talent. As we've seen, people are keen to work for mission-driven organisations. Creating a shared resource to find and keep great talent with scaling experience, as recommended earlier, will make it easy for more people to get and stay involved in social enterprise. In addition, a commitment to develop and progress that talent is critical. Designing structured learning and development within teams is necessary alongside on-the-job learning. This would include elements like shared curriculums; learning, development and progression offers; formal learning and development; opportunities for secondments; capability frameworks; performance management approaches; and reward strategies among other elements.

[211] https://www.bridgesfundmanagement.com/bridges-ventures-beats-target-with-75m-for-second-community-development-venture-fund/ (Accessed 14 May 2019)

[212] https://www.bridgesfundmanagement.com/what-we-do/ (Accessed 14 May 2019)

[213] https://about.beauhurst.com/accelerating-the-uk-report/#funding-stats

Building a stronger movement around social enterprise would also help de-risk social scaleups. Imagine the buying power of every social sector organisation being harnessed to support these organisations to flourish? Adopting the principles of the B-Corps movement and getting more social enterprises and charities to procure from each other, and make introductions to potential clients would unlock a force of nature.

Finally, market side initiatives from the public sector could also help, such as making contract sizes smaller and have more generous terms for businesses that value positive externalities (impact beyond the contract). The Social Value Act was put in place in January 2013 and requires people who commission public services to think about how they can also secure wider social, economic and environmental benefits. It is being implemented to different degrees across different commissioning bodies, and needs to be strengthened.

Confidence through Co-investment

Having a well-respected institutional investor commit an investment to a business gives other investors comfort that the lead investor has done its due diligence and believes in the potential of that business to thrive. In addition, increased transparency and data sharing between investors should work to reduce due diligence costs. If the lead investor is a hands-on type of investor, it also gives comfort to other investors that good levels of support will be given to the business. Co-investment programmes, such as the ones the EIF run alongside business angels and incubators through its EFSI Equity programme (see case study above), have the potential to provide greater comfort to individual investors around the robustness of a particular deal and crowd in more capital.

Co-investment not only signals confidence, but also materially reduces an investor's risk by reducing ticket sizes. By investing alongside other investors to make sure a deal happens each investor reduces their stake in the business, and thus their exposure.

Extended Time Horizons

Extended time horizons are important for social enterprises that might take longer than their commercial counterparts to grow. Most fund managers run time-limited funds, pressuring businesses to grow quickly and sell within that period.

A few existing investment structures eliminate this time pressure:

1. Holding Company. A holding company is a parent company that owns enough voting stock in other companies that it can control those companies' policies and oversee its management decisions. As it effectively owns other companies, it does not have to sell at a given time and creates value for its shareholders by growing the value of its underlying businesses. Examples of social holding companies include Groupe SOS, DCC, ProCredit Holding (Omidyar), and ResponsAbility.
2. Permanent Capital vehicle - on Balance Sheet. Rather than investors making investments from a fund with external investors that has a limited term, an investor can make investments using its own money, directly from its own Balance Sheet. This eliminates any time pressure on underlying businesses to grow at a certain pace or sell at a certain time. An example of this is BGF – see case study below.
3. Open-ended Fund. An open-ended fund is a type of permanent capital vehicle that can issue unlimited new shares that are redeemable, as opposed to a closed-ended fund that has a fixed number of shares that are not redeemable. The benefit to this is that it can always accept new investors, and its existing investors can theoretically exit at any time. This means that some underlying investments can be held for the long-term. Evergreen funds are a type of open-ended fund that are allowed to recycle capital after an exit, where open-ended funds distribute it to investors.
    a. Bridges Evergreen Fund provides long-term mission-aligned capital and support to organisations delivering high impact public services. The fund is targeting an initial size of £100m to reach sustainability with realisable income to begin attracting larger scale commercial institutional investors like Local Authority Pension Funds.

b. SASC Community Investment Fund is an evergreen fund that invests between £250,000 and £2m in community based, locally-led organisations providing support and services to improve the well-being of local residents, develop the local economy and create positive social change for everyone in the community.

c. Triodos Organic Growth Fund launched in January 2014. It is an evergreen fund that invests equity into non-listed sustainable consumer product companies in Europe, with a focus on organic food, sustainable clothing and textiles, and personal care.

Investment Trust. An investment trust is a form of closed-end fund. A company in its own right, it issues a fixed number of shares that investors can buy, and then trade between themselves. The management team buy and sell underlying assets, and can take a long-term view because the shares are not redeemable: the fund does not ever have to panic-sell, as shareholders need to find someone else to buy their shares to exit. Most investment trusts have an unlimited life.

Case study: BGF

BGF (formerly Business Growth Fund) is an investment partner for growing companies in every sector of the economy. It provides the tools SMEs need to grow, from funding to expertise, while letting them set their own course.

Established in 2011, BGF was born with the purpose to kick-start the UK economy. It takes non-controlling, minority equity stakes of initially between £2-10m into UK SMEs with turnovers between £5-50m. BGF invests directly from its £2.5b balance sheet, thus can hold its investments for the long-term as it is not restricted by short-term investment deadlines. BGF has become expert at investing in this stage of scaleup growth, and is happy for its investees to grow slow and steady, at around 10-15% per year. BGF invests using a combination of loan notes and ordinary shares, but always takes an equity stake to participate fully in any potential upside.

It also provides follows-on funding to support businesses' long-term growth. Its funding is underpinned by ongoing advice from its network of business leaders, and in-house support on senior appointments.

Over the past eight years BGF has deployed £1.7b into 280 portfolio companies, 25-30% of which are tech companies, and has had £2-300m returned. It typically does 30-40 deals per year, representing a third of the market for the type of deals they do, and invests where others don't. Because of its non-controlling long-term stake, it is able to have a different conversation with entrepreneurs and win their trust and business where they may not have otherwise sought finance from anyone else. That different conversation is more about partnership than what Private Equity is usually associated with (e.g. asset stripping) – leaving entrepreneurs in control, while able to follow-on and without a deadline for an exit.

Although BGF is a completely commercial entity and does not target or measure impact across its portfolio, it estimates around 18% of the entrepreneurs it has invested in are motivated by purpose as well as profit. One example is Evo Dental, a business providing life changing full jaw reconstruction for patients suffering from severe dental problems caused by advanced gum disease, congenital bone loss or accidents. They aim to make jaw replacements more accessible to those who can't afford them.

BGF has a staff of 150 people, half of which are investors, operating from 14 offices across the UK and Ireland.

Business Example: Third Space Learning is an EdTech venture using technology to tackle mathematical underachievement in schools, particularly for the most disadvantaged students. Its technology enables students to work one-to-one with a specialist maths tutor based in Sri Lanka via online video-chat classrooms. This helps students who would otherwise fall behind in class receive additional learning support.

Using a new technology and targeting a fragmented and budget constrained school customer base meant that investors without an impact motive were unlikely to be first movers. Third Space Learning's early investment rounds were supported by angel investors from the Clearly Social Angels network alongside support from the Wayra UnLtd incubator programme. Further growth investment was provided by Ananda Social Venture Fund and Nesta Impact Investments.

In the last four years, the company has worked with 16,000 children across 600 schools, delivering 200,000+ teaching hours and have grown to employ over 200 remote tutors in Sri Lanka. This track record and proof of demand from schools has meant the team were able to attract larger amounts of investment from Downing Ventures and UCL's Technology Fund to help accelerate their growth further.[214]

Fund Example: People in poverty or on low incomes often pay more for the same products or services than people who are better off financially. This is called the "Poverty Premium", the extra cost of being poor. Ascension Ventures runs the Fair by Design Fund, a fund designed as part of a wider programme with the goal of eliminating the poverty premium by 2028. The fund was launched in 2017 with £10m investment capital to invest in businesses of any legal form who are making a measurable dent in reducing the premium. Its Limited Partners, or investors, include Big Society Capital alongside a number of influential foundations such as the Joseph Rowntree Foundation, who bring deep insight into the drivers of poverty and the premium, and the Social Tech Trust who bring deep insight in investing in Tech for Good businesses. Alongside the fund, a campaign run by the Barrow Cadbury Trust is influencing the public, government, regulators, and corporates to put measures in place to stop the premium.

The fund invests in enterprises that are measurably reducing the poverty premium. These businesses have the potential to deliver market-rate returns, but given their target markets and the ethical way in which they do business, might struggle to raise commercial capital. The fund itself has struggled to raise commercial capital.

Recommendations

The recommendations made earlier in this paper to create a permanent scale readiness programme and scaling talent pools will not only help remove barriers to scale for social scaleups, but also help to de-risk them for investors.

Investment from impact investors can help prove these models, attracting commercial capital over time. Extended time horizons give these models the time to develop to their full potential, and create maximum value for investors. Some ideas include:

1. Publish research on the use of catalytic capital in the UK, highlighting where it has and has not been successful, in order to better understand and disseminate learning about how this capital can best be deployed, as well as inspire more owners of capital that could be catalytic of what's possible. This could demonstrate to asset owners the potential of investing in uncertainty. This should also include quantitative research to determine the size and nature of the capital need for segment A2 social scaleups to be better able to design future funding.
2. Make catalytic capital available to segment A2 businesses. New financing structures may be required to enable achievement of financial risk/return objectives. Following the research, work with mission-aligned funders, like Government and sector-specific foundations, who want to see these businesses scale up and are willing to pay for the impact and outcomes generated. This will mean playing a key role to ensure deals go ahead that wouldn't have otherwise, by de-risking other investors. Connect them to opportunities to deploy their catalytic capital by taking junior positions in funds struggling to close their fundraising rounds. This will work to crowd in much larger amounts of capital for this segment.

[214] Case study from Big Society Capital's Venture Paper (to be published) D. Sloan

3. Consider designing a guarantee scheme that reduces the risk in investing in social scaleups that have not yet proven their models.
4. Ensure that new funds have long time horizons that give social scaleups enough time to prove their models.
5. Consider designing a commercial fund to invest in B-Corps scaleups. This could have the potential to deliver market-rate returns, with little need for concessionary capital.

Segments B1 & B2

Problem: These are businesses that, due to their business models, will never be able to offer a market-rate return even if successful. The risk to invest in them is much greater than the return they could ever produce. Many commercial businesses fall into this segment and cannot access Venture Capital and Private Equity capital. If they are lucky enough to have or build strong networks, they may manage to secure investment from friends and family, who support the entrepreneurs despite low potential returns. Other support comes from government subsidies, through small business loans, guarantees, and tax breaks, and through generous terms in public outsourcing contracts.

If social enterprises in this segment are incapable of providing a risk-adjusted market rate return, what might make an investor accept a lower return? The potential of impact at scale. Either government or mission-aligned funders need to care enough about the impact the social scaleup can create. Investors pay for the promise of impact by accepting lower returns.

Regulated SEs: Many regulated social enterprises fall into this category – able to provide a return but not one high enough to attract commercial capital. For those who can't take on equity, quasi-equity and debt are the only options as financing instruments. Even if they succeed wildly, investors will only get a return that is a proportion of a metric, like profit or revenue. In this segment in particular, there is no opportunity to make big gains to offset other losses. To support high growth regulated social enterprises that cannot offer market-rate returns, by definition some sort of concessionary capital will be required.

A subset of regulated social enterprises operate in asset-heavy sectors, like transport, housing or manufacturing. They may be able to achieve slow steady growth through debt secured against their assets with little need for equity-like growth capital.

Case study: HCT Group

HCT Group is a social enterprise providing transport services and community services in Bristol, Guernsey, Jersey, London and Yorkshire. It has grown from £202k turnover in 1993 to employing over 1,500 people, having a fleet of 730 vehicles and a 2017/18 turnover of £62.9m. It has always increased its turnover, and grown on average 24% for 20 years.

History

Hackney Community Transport was formed in 1982, providing low cost minibuses for local community groups. In 1993, with traditional grants under threat, management decided that the best way to become sustainable was to become an enterprise. HCT began to compete for commercial contracts in the marketplace to ensure it could continue to provide community transport. Its first successful bid was a very small contract getting patients out of a hospital two days a week. And its very first Transport for London (TfL) contract was to run a mobility bus network in for London, before buses were accessible. HCT also campaigned for disability transport rights, and learned quickly that you have a stronger seat at the advocacy table if you deliver services too.

Over the course of two years, HCT built a relationship with TfL leading to its first red bus route, the number 153, which then represented 75% of its total turnover.

"We were terrible at delivery at first. The first month, we were bottom of the TfL service quality league table by a long way. I got called in to TfL for a tough conversation. Six weeks later we were mid table before rising to the top two and staying there." - Dai Powell, CEO

Dai's job for next 5 years was to diversify income by winning more contracts. Scaling the business was a seven-day a week job: Dai spent his weekends controlling buses.

Sector

HCT operates in the transport sector, specifically bus transport. This sector has some key characteristics that define its pertinence for high growth businesses: it is asset-heavy, with long-term contracts, a unionised workforce, low margins and a handful of large competitors with economies of scale. This translates to a business with not much room to manoeuvre on costs – implementing something like the London Living Wage has eluded them due to the need to compete on price with large players[215]. However, they do have assets against which commercial funders might lend, given their long-dated contracts, good cash flow from reputable quango (quasi-autonomous non-governmental organisations) counterparties and ability to repay.

[215] http://hctgroup.org/about_us/dai_powells_blog/43/I%20don%E2%80%99t%20believe%20in%20the%20Living%20Wage! (18 July 2014)

Finance

The first few contracts were financed through operating leases and a bank loan. TfL was a great counterparty because they would pay a majority of the contract up front providing good cash flow for a nascent business. When HCT reached around £15m turnover, it started having more conversations about how best to finance its activity. The question was: how should it finance if it wanted to carry on growing at a similar rate? In 2010, with £24m turnover, Bridges Ventures, Big Issue Invest, the Futurebuilders fund through Social Investment Business and Rathbone Greenbank together invested £4m into the company, which HCT said allowed for £20m of revenue growth.[216]

"Without social investment, our growth would have been slower. We wouldn't have been able to find the same level of headroom. If you can't take equity, banks will only do debt on a level of security. If you have enough security, you don't need a loan anyhow. We didn't spend it very well! We carried on growing fast, but didn't have the right internal structures to cope with the growth. We should've spent it faster. When we hit a hard time, if we hadn't had the investment, we would have gone bust. The cash made wobbly years easier to deal with." - Dai Powell, CEO

The round was financed through a Revenue Participation Note, with repayments to investors based on top line growth. In 2015, HCT raised a further £10m from social investors in a deal that included a social impact incentive feature, which allowed a reduction in the cost of borrowing if HCT met an agreed set of impact targets.

Equity is great because of the flexibility it affords, however HCT does not have high enough margins to be attractive to equity providers, and can't take on equity due to its charitable legal form. The most ideal finance, says Dai, would be a cheap revolving credit facility, or a charity bond guaranteed for 30 yrs. This type of long-term, affordable finance gives the team confidence to take up opportunities as they come, and not have to chase them or turn them down. Fundraising costs time, effort and fees.

Future Growth Plans

HCT has the opportunity to become very big. It doesn't want to change legal structure, as it wants to ensure its social mission remains on track and that it, itself, remains for the long term. This year, HCT bought two commercial transport companies and turned them into social enterprises. It could build up its cash reserves and grow organically, but to Dai, that "doesn't sound much fun".

Solutions: The only possible investors for this segment are those who will accept a sub-market rate of return for the promise of impact. The most likely to pay for the impact are those who share impact objectives with the business, or government departments who have specific mandates and budgets aligned to the impact created. To get capital, these businesses must find the funders who care most about the impact they are creating, and must be able to provide robust evidence demonstrating that impact. This makes blanket solutions hard to design, while issue-specific targeted solutions will only ever serve a subsection of those in demand for investment.

As the demand for this type of funding is so high, suppliers of funding set the rules and control the flow to causes they care about most. Finding sectors that have many scale-ready social enterprises can help crowd in larger amounts of coordinated funding into one theme, especially from government departments who might struggle to fund in small, fragmented amounts. The key task is understanding which areas are scale-ready, and also fit priorities of different funders.

What is needed is either long-term provision of subsidy, in the form of either grant, blended finance, repayable grants, or guarantees (as grants) that bring in commercial capital, or long-term concessionary capital happy with a reduced level of return.

[216] https://www.thirdsector.co.uk/hct-group-raises-10m-largest-impact-investment-deal/social-enterprise/article/1375957 (Accessed 27 Jan 2019)

Investors in segment B can either give grants to sit alongside commercial investment to de-risk them (blended finance), or make repayable investments which will not deliver a market-rate return. There are four groups of stakeholders who might be willing to do this:

1. Mission-aligned foundations;
2. Venture Philanthropists and Impact Investors, who seek concessionary returns;
3. Government departments and Local Authorities, where the social enterprise is creating social value either for the policy area or geographic area it is concerned with; and
4. Individuals with either small (retail investors) or large (High Net Worth Individuals HNWIs) amounts of money.

Foundations

Foundations give millions in precious grants per year. Some also make social investments that are repayable. Foundations with flexibility in their return expectations have the potential to provide catalytic capital, enabling impact to happen sustainably at a large scale. In fact, six in ten foundations principally target below-market-rate returns in their social investment portfolios.[217] Particularly in segment B, social enterprises can only grow their impact to a larger scale using concessionary funding. Foundations with missions aligned to those social enterprises are well placed to provide that growth funding.

Foundations sometimes do not wish their funding to be seen to "subsidise private gain", or ensure commercial investors achieve market-rate returns, which they may consider to be outsized. If a foundation chooses not to deploy its capital in this way, the alternative may be for the social enterprise not to access large enough amounts of capital and struggle to grow. Consequently, their Impact will remain small or potentially non-existent if the business folds.

Example: Catalytic Capital Consortium

Catalytic Capital Consortium

The Catalytic Capital Consortium is "an investment, learning, and market development initiative bringing together leading impact investors who believe that greater, more effective use of catalytic capital is an essential component of achieving the Sustainable Development Goals (SDGs) and realizing the full potential of the impact investing field." Conceived of by the MacArthur Foundation, in partnership with Omidyar Network and Rockefeller Foundation, it is dedicating up to $150 million to invest on a matching basis in approximately five funds or intermediaries that demonstrate a powerful use of catalytic capital across sectors and geographies. They define catalytic capital as "investment capital that is patient, risk-tolerant, concessionary, and flexible in ways that differ from conventional investment".

Venture Philanthropy (VP) and Impact Investors

The European Venture Philanthropy Association (EVPA) defines venture philanthropy (VP) as "an approach to building stronger investee organisations with a societal purpose, by providing them with both financial and non-financial support. VP's ultimate objective is to achieve societal impact. It does this through both social investment and high-engagement grantmaking." The EVPA has more than 275 members from over 30 countries. According to the EVPA's annual survey, in FY 2017, Venture Philanthropy and Social Investment organisations invested €767 million to support 11,951 social purpose organisations, with VP organisations investing €7.8 million in total on average[218].

Venture philanthropy comprises of tailored finance, non-financial support and impact

[217] 2018 GIIN Annual Impact Investing Survey https://thegiin.org/research/publication/annualsurvey2018

[218] https://evpa.eu.com/pages/webinar-key-trends-and-results-on-european-investors-for-impact-the-evpa-survey-2017-2018 (Accessed 21 April 2019)

management/measurement. From the finance provided, there is an expectation of some financial return or partial capital preservation. Almost half of the financial support provided by European Venture Philanthropy Organisations is deployed through debt instruments (49%) followed by grants (29%), equity (16%), and hybrid instruments (5%). Hybrid instruments include quasi-equity and:

> *Match Trading* – matching a portion of turnover with grants, often used to incentivise entrepreneurs to increase their turnover from one year to the next.

> *Convertible loans* – loans that may be converted into equity, useful when a venture is too young to value, making the price of equity difficult to determine at that time

> *Recoverable grants* – loans that may be converted to a grant under certain circumstances (i.e. failure of the business or pilot). [219]

According to the Global Impact Investing Network's (GIIN) Annual Investor Survey, 36% of all impact investors are targeting below market-rate returns. Most non-profit fund managers target below-market returns (70%).[220] This proves that "impact-first" investors do exist and will prioritise impact return over financial return. A measurable impact is therefore critical.

[219] Ibid

[220] 2018 GIIN Annual Impact Investing Survey https://thegiin.org/research/publication/annualsurvey2018

Case study: Education: Ark & Ambition School Leadership (£194m turnover, £20m excluding Ark Schools)

Segment: B1/B2/C

Ark is an international charity, transforming lives through education. It exists to give every young person, regardless of his or her background, a great education and real choices in life. In the UK, it has a network of 38 schools, educating around 26,000 pupils in areas where it can make the biggest difference. Through Ark Ventures, it incubates, launches and scales initiatives that address some of the most intractable issues in education and society – in the UK and around the world. These include STIR and Frontline, now legally independent organisations, and Assembly that was sold in a trade sale. Ed City, Education Partnerships Group, English Mastery, Maths Mastery and Now Teach remain part of Ark.

Ambition School Leadership (Ambition) was formed in 2016 when an Ark venture, Teaching Leaders, merged with the Future Leaders Trust. It provides world-class leadership development and technical training to educators in England and Wales. Ambition has a turnover of between £16-20m (on top of Ark's £194m as it is now a legally independent organisation), and employs approximately 200 staff. It is in the process of merging with the Institute for Teaching.

Insights

1. Ark run a venture programme, with a very high bar for investment (e.g. grants or interest-free loans). The team doesn't have any deployment targets as they don't manage a fund or specific pot of capital – they only invest when they have a very high level of confidence and currently fundraise for each venture individually. They don't invest assuming they'll back ten and only one will succeed. They do not invest to make financial returns - their aim is for ventures to be sustainable on earned income. Each venture needs the potential to produce systemic change, and have a route to financial sustainability. Incubated organisations are typically part of Ark, only spinning out at a later point.
2. Flexibility and Non-financial support are critical: once a venture is in the family, Ark gives them what they need to succeed, such as an operational backbone (HR, finance support, desk space), strategic support, and will fill gaps in team when required. They have a team of Venture Partners - often ex-consultants or social enterprise COOs - employed to give entrepreneurs support in financial modelling and business case development (the main skills they find lacking in social entrepreneurs), operations, systems, and processes. Ark also provides back office support, and can give parent company guarantees for leases or contracts. ASL wouldn't have scaled nearly as fast as it did without Ark as guarantor on their leases.

3. Ark requires a large degree of ultimate control over the social ventures in which it invests. If Ark invests in an organisation, they are legally part of Ark for the period of incubation. Once they finish the period of incubation they typically spin out. Some ventures are unlikely to ever spin out due to their close links to Ark schools. This spin out process has happened with a range of ventures including Ambition, Frontline, STIR and Assembly.
4. After spin out, Ark remains involved and supports ventures to continue to grow (i.e. encouraging and then helping Teaching Leaders, Future Leaders and The Institute for Teaching to merge).

Government

Government has a vested interest in seeing social enterprises scaleup: it is often trying to solve the same challenges in different but complementary ways. It has many tools at its disposal to help social enterprises scale up. We have already discussed the market-side initiatives government could undertake such as smaller contract sizes and ensuring the Social Value Act is strengthened and used appropriately. Government also has the power to intervene in certain sectors to ensure they survive and thrive. Government can play multiple roles to support social enterprises in this segment, as:

> investors through grants, repayable concessionary investment, or guarantees as grants;

> procurers; and

> policy-makers.

We previously looked at how guarantees might work to support increased commercial investment in segment A businesses. They could also be used to support more investment into segment B businesses, albeit at a much higher cost as they will be much more likely to be called.

There are many examples where government has intervened to scale areas it deemed to be of importance. It provides at least £7.5 billion in annual subsidies to SMEs[221].

Feed-in-Tariffs were a subsidy introduced by government in 2010 to encourage the installation of renewable energy generation assets. Prior to the subsidy, it did not make economic sense to install the assets as the costs were too high and revenues too low. By increasing revenues of that business model, government incentivised the installation of almost 5 GW of solar, 725 MW of wind, 220 MW of hydro, and 289 MW of anaerobic digestion capacity[222].

The renewable heat incentive (RHI) is a long-term financial support programme for renewable heat implemented by BEIS and Ofgem. The RHI pays domestic households, mainly off the gas grid, since 2014 and non-domestic organisations since 2011 to generate and use renewable energy to heat their buildings. By increasing the generation of heat from renewable energy sources instead of fossil fuels, the RHI helps the UK reduce greenhouse gas emissions and meet targets for reducing the effects of climate change[223].

Following the financial crisis in 2008, many house builders were left with unsold stock. Government stepped in to purchase that stock through a newly created National Clearing House, and took houses on as affordable housing through Housing Associations[224].

Government has also introduced tax reliefs for specific sectors in the past, such as the Small Brewer Relief introduced in 2002. This tax relief reduces duty owed on beer production by up to 50%, and helps breweries producing less than 60,000 hectolitres per year establish themselves and compete with larger producers[225]. The creative industries also benefit from a set of eight

[221] This calculation includes around £4 billion in annual tax subsidies, £9 billion to Local Enterprise Partnerships over three years (2014-2016), and Start-Up Loans of about £66 million per year. Due to lack of detailed information, it excludes £3.2 billion of Regional Growth Funding over 6 years (2011-2017), Enterprise Finance Guarantee, Venture Capital Catalyst Programme, SME discounts on the Apprenticeship Levy Scheme, UK Export Finance, £12m per year on Growth Hubs, Childcare Business Grants Scheme, Innovation Vouchers and Catapult Centres from Innovate UK, New Enterprise Allowance among others.

[222] https://www.ofgem.gov.uk/environmental-programmes/fit/contacts-guidance-and-resources/public-reports-and-data-fit/feed-tariffs-quarterly-statistics (Accessed 15 May 2019)

[223] https://www.gov.uk/government/publications/2010-to-2015-government-policy-low-carbon-technologies/2010-to-2015-government-policy-low-carbon-technologies#appendix-6-renewable-heat-incentive-rhi (Accessed 18 May 2019)

[224] http://www.uk-housing.co.uk/HMD/ARCHIVE/09/01/1400/ (Accessed 18 May 2019)

[225] https://www.morningadvertiser.co.uk/Article/2018/04/10/Beer-duty-change-proposals-spark-fears-of-price-hikes-and-brewery-closures (Accessed 18 May 2019)

tax reliefs for organisations directly involved in the production and development of: certain films, animation programmes, high-end and children's Television programmes, video games, theatrical productions, orchestral concerts, and museum or gallery exhibitions[226].

Individuals

Individual people care deeply about a range of issues, and already part with their money through donations to see impact: 60% of people say they have donated money in the last year, with an estimated total of £10.3 billion donated in 2017[227].

Retail investors already invest locally into community shares, supporting local initiatives to improve their communities such as pubs and village shops. Over £130m has been raised through this type of equity in the UK to date[228]. There are many platforms that allow individuals to give or invest small amounts of money to the causes and businesses they care about. Some examples of these include Just Giving, Kickstarter, Crowdfunder, Spacehive, Kiva, Abundance and Ethex to name a few.

For individuals with larger amounts of money to invest or donate, Donor-Advised Funds (DAF) and SITR funds are options. A DAF allows people to donate amounts of money whenever they want, receive tax benefits immediately, and determine how to spend those funds over time. These funds can be used to make social investments as well as grants, as long as the capital is never returned to the donor and remains in the DAF, recycled to make more social investments over time.

> "I initially made a £1.5 million allocation for social impact investment through my DAF account. Since then, the funds have been recycled many times, so that my initial investment has enabled a total commitment of £6.6 million in more than 400 deals."
>
> - Sir Harvey McGrath

SITR funds allow investors to invest a large chunk of capital into many social enterprises and receive 30% of their capital back up front through tax relief through a fund structure. Minimum investment amounts vary but usually start at £10,000. Concessionary capital SITR funds could be created for those investors who care about seeing impact at scale in a specific sector, and are willing to forgo a market-rate level of return. The tax relief would go a little way towards protecting their capital as well.

Recommendations

This report has focused on gathering learning from the commercial sector. Drawing from that learning, we have discovered that an A2 scaling fund might work really well. However, we have also learned how difficult it is to get any kind of capital to businesses in segments B1 and B2. We know subsidy needs to be used, but exactly how that subsidy can be delivered will be up to the institutions and individuals who have concessionary capital to deploy to achieve specific impact.

Some recommendations and approaches identified above that can better support A2 segment businesses are applicable to Bs as well. These include implementing measures to de-risk them, providing guarantees, giving confidence through co-investment and allowing longer investment time horizons. However these alone will not be enough for this segment.

Making the right kind of capital available is critical. Some ideas for investors looking to have outsized impact by investing concessionary capital include:

1. Creating sector-based alliances of funders, who collate best practice approaches to maximising impact, and, taking a systems-based approach, can test and pilot new initiatives. These alliances could result in targeted, sector-focused funds that provide a blend of concessionary and commercial capital to get to a viable scale quickly. The priority sectors identified and explored in this paper would be good places to start.

[226] https://www.gov.uk/guidance/corporation-tax-creative-industry-tax-reliefs (Accessed 18 May 2019)

[227] Charities Aid Foundation UK Giving Report 2018 https://www.cafonline.org/about-us/publications/2018-publications/uk-giving-report-2018 (Accessed 18 May 2019)

[228] https://communityshares.org.uk/open-data-dashboard (Accessed 18 May 2019)

2. Supporting platforms that make it easier for individuals to find and invest in the causes and businesses they care most about.
3. Concessionary capital can be used to support large social enterprises wanting to bid for stretch contracts and tenders, providing:
    a. Pre-bid scale readiness finance and support
    b. Guarantees to support their bids
4. A pool of concessionary capital to support a range of segment B social scaleups across different sectors would be a very important initiative with potential to provide many benefits. Given the amount of capital needed to scale even just one business, an initiative like this would need a significant amount of government funding that doesn't at the moment seem aligned to current policy areas or siloed departmental budgets.

Conclusions

Access to capital remains one of the most important barriers for social scaleups, due to a range of factors. However enabling this capital to flow will require different approaches for different types of social scaleup. They can be categorised using Omidyar Network's framework into six segments – each with a potential to deliver a different level of returns for investors.

As we have learnt, it is easier to fund asset-backed businesses who grow by acquiring more assets, as they pose less risk to investors. It is harder to fund enterprise growth that is not reliant on assets. Funding regulated social enterprises depends more on their ability to create profit, and thus what segment they belong to, rather than legal or funding structures, or products. If investors can find a group of regulated social enterprises they believe have potential to deliver market-rate returns, they can structure funding around their legal requirements.

For Segment A2 ventures, impact investment can be used a catalyst to help ventures prove their models. For Segment B1 & B2 ventures, concessionary capital is a necessity.

Going after Scale with Scale

One thing often repeated is to go after scale with scale. Creating scaleups takes monumental effort: time, energy and resources. But the prize of impact at scale, improving millions of people's lives is worth it. This section explores a few funding initiatives who are taking that advice to heart – both in terms of scaling social innovation and scaling enterprises.

European Innovation Council Pilot (2018-2020)

With only 7% of the world's population, Europe accounts for 20% of global R&D investment, produces one third of all high-quality scientific publications, and holds a world leading position in industrial sectors such as pharmaceuticals, chemicals, mechanical engineering and fashion. But Europe needs to do better at turning that excellence into success, and generating global champions in new markets based on innovation. This is particularly the case for innovations based on radically new technologies (breakthrough) or markets (disruptive)[229]. Compared to the EU's €6 billion in venture capital, the US has €38 billion[230]. Today, of the world's 15 largest digital firms, not one is European[231].

In June 2018, the European Commission published a proposal for Horizon Europe, a €100 billion research and innovation programme for 2021-2027 following on from the €80 billion Horizon 2020 (2014-2020). Part of the recommendations was to create a permanent European Innovation Council (EIC), set up under the next long-term budget (2021-2027).

The Enhanced European Innovation Council (EIC) pilot aims to support top-class innovators, start-ups, small companies and researchers with bright ideas that are radically different from existing products, services or business models, are highly risky and have the potential to scale up internationally. The pilot phase offers €2.7 billion in funding for the period 2018-2020 (financed through existing Horizon 2020 budgets), opportunities for networking, mentoring and coaching and strategic advice to upgrade the innovation ecosystem in Europe.

The EIC pilot is able to support ideas from any area of technology or business sector, including novel combinations of technologies and business models, such as artificial intelligence, biotechnology and zero-emission energy. Support is available from feasibility stage (e.g. proof of concept or development of business plans) to development to scale up stages.[232]

Blue Meridian Partners

Blue Meridian Partners is a group of philanthropists who seek to transform the life trajectories of children and youth living in poverty across America. Blue Meridian identifies, invests in and scales up the most promising strategies poised to make a national impact on solving the social problems confronting poor children and youth. Blue Meridian's partnership structure allows its partners to pool their philanthropic resources and invest more effectively and efficiently than they

229 http://europa.eu/rapid/press-release_IP-19-1694_en.htm (Accessed 21 March 2019)
230 https://www.euractiv.com/section/economy-jobs/news/european-innovation-council-ramps-up-with-improved-pilot-phase/ (Accessed 21 March 2019)
231 https://europeansting.com/2019/03/18/europe-is-no-longer-an-innovation-leader-heres-how-it-can-get-ahead/ (Accessed 21 March 2019)
232 https://ec.europa.eu/programmes/horizon2020/en/h2020-section/european-innovation-council-eic-pilot (Accessed 21 March 2019)

could individually. Each of Blue Meridian's General Partners commits at least $50 million over five years and Blue Meridian has raised over $1.7 billion to date.

Blue Meridian's large-scale investments carry commitments of up to $200 million over 10–12 years. These investments are approved in two to four year phases with annual pay-out based on meeting performance milestones.[233]

Co-Impact

Co-Impact is a global collaborative for systems change launched in November 2017, focused on improving the lives of millions by advancing education, improving people's health, and providing economic opportunity. It has promised to distribute an initial $500m to this cause[234], and its core partners include Richard Chandler, Bill and Melinda Gates, Rohini and Nandan Nilekani, Jeff Skoll, and The Rockefeller Foundation.

Co-Impact grants are typically $10 to $50 million USD over five years, accompanied by non-financial support, and customized to provide programme partners with operational flexibility needed to achieve impact. Co-Impact look for initiatives that are poised to achieve breakthrough results at a national or regional level. Rather than scaling the direct service work of individual NGOs, it supports systems change plans that are designed and executed with partners critical to long-term success at scale, including community groups, government, other NGOs, and the private sector.[235]

100&Change Initiative

100&Change is a MacArthur Foundation competition for a $100 million grant to fund a single proposal that will make measurable progress toward solving a significant problem. The first award was granted in December 2017 to Sesame Workshop and the International Rescue Committee, which educates young children displaced by conflict and persecution in the Middle East.

https://ssir.org/articles/entry/seeking_both_problems_and_solutions

https://www.100andchange.org/#about

Global Innovation Fund

Launched in 2014, the Global Innovation Fund invests in social innovations that aim to improve the lives and opportunities of millions of people in the developing world. It exists to fund innovations that have the potential to scale to reach millions of people. A unique hybrid investment fund, it supports the piloting, rigorous testing, and scaling of innovations targeted at improving the lives of the poorest people in developing countries. By mid-2017, GIF had invested $56m in 32 partnerships[236].

Through grants, loans (including convertible debt), and equity investments ranging from $50,000 to $15 million, GIF backs innovations with the potential for social impact at a large scale, whether they are new business models, policy practices, technologies, behavioural insights, or new ways of delivering products and services that benefit the poor in developing countries.[237]

Catalyst Fund

Catalyst Fund supports early-stage ventures targeting low-income customers in emerging markets. Managed by BFA, the program was founded in 2016 with the support of the Bill & Melinda Gates Foundation and JPMorgan Chase & Co.

"All around the world, entrepreneurs are trying to solve meaningful problems experienced by people on low incomes. But they can't do it alone – early-stage innovation can't scale without access to flexible capital, the right tech, product, and customer expertise in emerging markets, and critical connections to investors.

"Catalyst Fund works closely with inclusive FinTech start-ups to de-risk their early stages. It helps start-ups shorten their time to product-market fit, validating products or services low-income customers want and that can become viable businesses, and raise funding from later-stage investors.

"Since 2016, Catalyst Fund has deployed $2m USD in grants and $1m USD in bespoke advisory services to 20 global start-up enterprises. Catalyst

[233] https://www.bluemeridian.org
[234] https://www.ft.com/content/b9487e30-c951-11e7-aa33-c63fdc9b8c6c
[235] https://www.co-impact.io/whatwefund/
[236] Global Innovation Fund 2016/17 Impact Report
[237] https://globalinnovation.fund/

Fund companies raise on average $1m USD after the program."[238]

Innovation Investment Alliance

In 2012, USAID's U.S. Global Development Lab and the Skoll Foundation partnered to launch the USAID-Skoll Innovation Investment Alliance (IIA) to influence systems-level change by supporting proven, transformative, and innovative organizations to reach scale. The IIA will measure, analyse, and share findings from partners to influence broader change within communities aiming to solve pressing global challenges.

The IIA has invested almost $50 million in eight proven, transformative social enterprises to scale their impact. It aims to create systems-level change across sectors and geographies, and draw out lessons on scaling that are applicable to the social enterprise community and inform the ongoing conversation on how to create sustainable impact at scale. These investments are: Imazon, VisionSpring, Evidence Action, WSUP Advisory CIC, Proximity Designs, One Acre Fund, Fundación Capital, and Living Goods.

[238] https://catalyst-fund.org/

Conclusions

Social enterprises play a critically important role in addressing some of our most important challenges. They are proving there is a new way to do business, one that creates value for many more people than solely shareholders. They create employment, they are significant contributors to GDP and they intend to have impact way beyond both of these key metrics.

Social enterprises in the UK are numerous and sizable. They appear to be performing well compared to commercial SMEs across many categories, but do struggle to export and raise patient growth finance over £1m. There is a lack of robust data on the state of social enterprise. Addressing this needs to be a priority given the vital importance of this sector of business to the UK economy and society.

Social enterprises do struggle to scale, but so do commercial companies with only a very small proportion ever reaching a large size. Social enterprises face all the normal barriers to scale, as well as a host of other barriers specific to their unique characteristics. In particular, they face barriers to scaling up the quality of their impact in parallel with the size of their businesses. The ability to do this is critical to achieving impact at a large scale, and realising the potential of social enterprise to deliver real social and environmental value, alongside jobs and economic growth.

Many support programmes exist to help businesses reach scale. While the ScaleUp Institute endorses support programmes for commercial scaleups, only a handful exist that specifically focus on social scaleups. One critical area of support identified is the concept of 'scale readiness': ensuring a business has the right team, systems, processes and policies in place to be able to respond to more diverse and bigger opportunities. Becoming scale-ready could take up to two years to achieve, depending on the business. In order to have the best chance of scaling up, businesses need this vital support. Support programmes for social enterprises need to build on or be linked to what we learn works for commercial businesses, with additional support to overcome barriers unique to the social sector.

Although social scaleups can exist in many sectors, there are certain sectors where social enterprise models are a natural fit – particularly those sectors where the product or service has an inherent impact, like healthcare, housing and education. If an coalition of funders and other interested parties were to take a strategic view that having many scaled up social enterprises was an important outcome, these are the sectors where they might start.

This paper puts forward a bold vision to see **one hundred more social enterprises reach scale across a range of priority sectors in the next five years.** It identifies eight critical areas of support needed to turn this vision into a reality and makes suggestions on how those could be implemented.

Finally, to achieve scale will require a substantial amount of capital. A helpful framework is the Returns Continuum created by Omidyar Network. Using their segmentation, we can look at how to get capital to different types of social enterprises depending on their ability to generate impact, profit and market-rate returns. Those in Segment A should be investable using existing social investment infrastructure in the UK if it were to be better capitalised with enough scale to meet the challenge of delivering many scaled enterprises.

There is a clear need and role for concessionary capital. Those in Segment B who will never have the potential to deliver market-rate returns find it harder to get investment. Their only potential investors are those willing to pay for the impact generated at scale by accepting a lower return. It is likely that such an investor would be motivated to put their precious capital towards addressing specific issues, rather than to see social enterprises operating at scale in general, thus blanket solutions remain difficult to design.

It is critical to find investors with concessionary capital to ensure deals in both segments can get finance. In Segment A, catalytic investors can play a vital role in ensuring funds raise enough funds by taking junior positions, while having a good chance at achieving a good return. In segment B, concessionary capital is the only way these businesses will reach any sort of scale. Backing platforms that make it easier for individual investors, both retail and sophisticated, to invest concessionary capital in social enterprises delivering outcomes in areas they care about is an area of great opportunity.

In addition to amassing the right kinds of capital at the right scale, other interventions could be used to attract investment, such as taking actions to de-risk ventures (like scale readiness), guarantees, and tax breaks.

A UK with more, scaled up social enterprises operating across many sectors would be a richer one in more ways than one.

Appendix I: Agency Social Enterprise Definitions

Social Enterprise UK (SEUK), the UK's membership body for social enterprise, defines it by the following common characteristics:

> An enshrined primary social or environmental mission, through legal form, governing documents or ownership for instance;

> Principally direct surpluses towards that mission;

> Independent of government; and

> Primarily earn income through trading, selling goods or services.

The **European Commission** (2011) interprets a Social Enterprise as "an operator in the social economy whose main objective is to have a social impact rather than make a profit for their owners or shareholders. It operates by providing goods and services for the market in an entrepreneurial and innovative fashion and uses its profits primarily to achieve social objectives. It is managed in an open and responsible manner and, in particular, involves employees, consumers and stakeholders affected by its commercial activities."[239]

The **European Investment Fund** (EIF), and others, argue that there doesn't necessarily have to be a trade-off between purpose and profit. Their revised definition, used for the Employment and Social Innovation Guarantee Financial Instrument (EaSI GFI) is as follows:

"Social Enterprise' means an undertaking, regardless of its legal form, which:

1. in accordance with its Articles of Association, Statutes or any other statutory document establishing the business, has as its primary objective the achievement of measurable, positive social impacts rather than generating profit for its owners, members and shareholders, where the undertaking:
   a. provides services or goods which generate a social return and/or
   b. employs a method of production of goods or services that embodies its social objective;
2. uses its profits first and foremost to achieve its primary objective and has in place predefined procedures and rules for any circumstances in which profits are distributed to shareholders and owners, in order to ensure that any distribution of profits does not undermine the primary objective;
3. is managed in an entrepreneurial, accountable and transparent way, in particular by involving workers, customers and/or stakeholders affected by its business activities."

The **Departments for Culture, Media and Sport (DCMS) and for Business, Energy and Industrial Strategy (BEIS)** conducted a full review into social enterprise definitions for their Social Enterprise: Market Trends 2017 research paper as follows.

Income:	Share of income from trading/commercial activities at least 50 per cent.
Use of Surpluses/Profits:	Rules/restrictions to use surpluses/profits chiefly to further social/environmental goals or past surpluses/profits are chiefly used to further social/environmental goals.
Organisational Goals:	Type of social or environmental goals that the organisation/business has and whether social/environmental goals are of greater or equal concern compared to financial goals.
Charitable status & legal form	Using the standard SBS questions asking for charitable status and legal form.

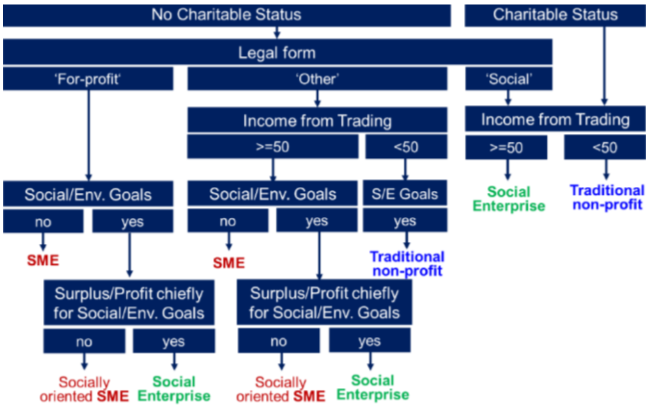
The report identifies three distinct types of social organisation:

1. **Traditional Non-Profit:** organisations that pursue social goals but generate less than 50% of their income from trading activities
2. **Socially-Orientated SME (or 'Mission-led businesses'):** enterprises that have social and/or environmental goals and generate their income chiefly from trading activities but do

[239] http://ec.europa.eu/growth/sectors/social-economy/enterprises_en

not use their surplus/profit chiefly to further those social/environmental goals

3. **Social Enterprises:** enterprises that have social and/or environmental goals, generate their income chiefly from trading activities, and use their surplus/profit chiefly to further those social/environmental goals



BSC defines for-profit social enterprises through its governance agreement that includes the following conditions:

> Mission enshrined in Social Objects;

> 50% cumulative cap on distribution of profit;

> Reasonable, proportionate remuneration of staff; and

> Make best efforts to preserve mission on exit.

BSC also stipulates that ventures should consider, measure, report and evaluate their impact. Often, intermediaries are relied upon to make a subjective judgement as to whether or not a for-profit commercial company is indeed a social enterprise, given their mission, activities, ethos, values, and employee and founder motivations. This works well in practice as intermediaries develop the skills to identify businesses making a real impact as genuine social enterprises. However **if social enterprise is to enter the mainstream, it must be made a lot easier to spot one for the general public.**

The **Social Enterprise Mark CIC** was launched in 2010, and is an international social enterprise accreditation authority. Its accreditations ensure that business models remain ethical, credible and commercial. It provides a standard for the social enterprise sector defining what it means to be a genuine social enterprise. It claims to have developed sector-agreed criteria as follows:

> Primarily dedicated to social and/or environmental objectives

> An independent business

> Earn at least 50% of income from trading

> A principal proportion of any profit (at least 51%) made by the business must be dedicated to social/environmental purposes

> Must distribute residual assets for social or environmental aims, if the organisation is dissolved

> Must demonstrate that social/environmental aims are being achieved[240]

According to the SEM directory, there are currently only 133 accredited businesses, including six from abroad. Given there are at least 100k social enterprises in the UK[241], this accreditation is not working.

[240] https://www.socialenterprisemark.org.uk/about-us/#toggle-id-1

[241] SEUK, Hidden Revolution: Size and Scale of Social Enterprise in 2018, 2018

Appendix II: Patient Capital Review Results

The result of the Patient Capital Review is that a £20bn package over the next 10 years will be delivered to support investment in innovative UK companies. The announcements in Chancellor Hammond's Autumn Budget in 2017 resulting from the Review include:

Tax relief changes:

> Doubling the annual allowance for investors in knowledge-intensive companies through the Enterprise Investment Scheme (EIS) to £2 million

> Doubling the annual investment that knowledge-intensive companies can receive through the EIS and Venture Capital Trusts (VCT) to £10 million

> Introducing further flexibility for these companies over how the 10-year maximum company age test for the first investment is applied

> The Treasury will introduce a test to prevent investments in low-risk companies through these schemes, potentially targeting that money to truly innovative sectors

> The R&D expenditure credit is to be increased to 12% (from 11%), which will benefit companies that have received R&D grants from the government and larger companies (SMEs already enjoy a 33% rate)

> Founding shareholders will be able to keep their relief on capital gains made during the period that they held over 5% of company shares before being diluted during funding rounds. The details will be consulted on next year.

New investments:

> A £2.5bn fund called British Patient Capital will be established in the British Business Bank (BBB) to invest in innovative companies, this will be a co-investment fund with private finance and will be floated or sold once it has a proven track record

> A series of funds of funds will be established with a first £500m tranche invested through the BBB and then at least a further two similar investments over the next 10 years

> First-time and emerging fund managers will continue to be supported through the British Business Bank's existing Enterprise Capital Fund programme

> A new knowledge-intensive EIS approved fund structure will be consulted upon, with further incentives provided to attract investment.

> The government stands "ready to step in to replace EIF funding if necessary"

Pensions:

> The Pensions Regulator will provide clarity around the ability of pension fund managers to invest in venture capital and innovative companies

> The government will address barriers holding back Defined Contribution pension savers from investing in illiquid assets, such as private companies[242]

[242] https://www.bioindustry.org/news-listing/autumn-budget-2017-analysis.html

Appendix III: Detailed Sector Analysis

A long list of 94 sectors was whittled down to twenty which were analysed based on their overall profitability, potential for growth, barriers to entry, buyer and supplier power, existing social sector activity and existing high growth commercial company activity. This analyses was then used to determine seven top sectors where social enterprises might have a strategic advantage in scaling up, as described in the main paper.

Sector Suitability

In order to get to a list of viable, strategically important sectors for scaled up social enterprise, value judgments had to be made about which sectors are most compatible and which are unsuitable. This involved a certain level of personal opinion, which was unavoidable. Readers may disagree with my conclusions; however, I had to draw the line somewhere in order to get down to the sectors with the best strategic fit.

From a long list of 94 sectors[243], eleven were removed because of their overall negative impact such as extreme negative environmental impact, military involvement and negatively impacting human health: Aerospace/Defence; Air Transport; Coal & Related Energy; four oil and gas sectors; Metals and Mining[244]; Precious Metals; and Tobacco. These sectors are considered less ethically suitable for social enterprise models, although there do exist a few.

Despite alcoholic beverages proven detrimental to one's health[245], the UK's Chief Medical Officer has published low-risk drinking guidelines[246], suggesting some consumption is acceptable versus Tobacco consumption, where the UK government is implementing a national effort on tobacco control and are aiming to achieve the first smoke-free generation[247], and was therefore not excluded. There are a number of scaling social enterprises operating in this category, such as Ginerosity (donate some profit to support disadvantaged young adults find work, training and education opportunities), Toast Ale (brews beer using surplus bread and donates all profits to food waste charities), Brewgooder (donates all profits to clean water charities), Two Fingers Brewing (donates all profits to Prostate Cancer), and Ignition Brewery (employs and trains people with learning disabilities to brew and serve beer), among others[248].

Twenty of the 94 sectors were determined to meet an essential need or the product or service has an inherently positive impact on people in need or the planet. Many of them could be considered to have negative impact, but that is due to the way they are operated rather than the product or service itself. These sectors are:

- Banks (Regional) - credit
- Drugs: - massive health benefits
  - Biotech
  - Pharmaceutical
- Education
- Environmental & Waste services
- Farming & Agriculture
- Green & Renewable Energy
- Healthcare:
  - Products
  - Support Services
  - IT
- Homebuilding
- Insurance (General)
- Publishing & Newspapers

[243] All data in this and following sections used gratefully from Professor Aswath Damodaran, Professor of Finance at NYU's Stern School of Business 5 Jan 2019 release of raw data on all 6,766 publicly traded companies in Western Europe, 1,328 of which are from the United Kingdom. http://people.stern.nyu.edu/adamodar/New_Home_Page/datacurrent.html More on Prof Damodaran here: https://www.forbes.com/sites/kevinharris/2018/07/17/professor-aswath-damodaran-on-valuation/#1d809585722c

[244] Mining industry and sustainable development: time for change, Fernando P. Carvalho https://onlinelibrary.wiley.com/doi/full/10.1002/fes3.109

[245] https://www.drinkaware.co.uk/alcohol-facts/health-effects-of-alcohol/

[246] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/545937/UK_CMOs__report.pdf

[247] Towards a Smokefree Generation, the Tobacco Control Plan for England 2017-2022 (July 2017) https://www.gov.uk/government/publications/towards-a-smoke-free-generation-tobacco-control-plan-for-england

[248] https://www.iridescentideas.com/blog/fancy-a-drink-this-weekend-here-are-our-top-ten-social-enterprise-alcoholic-drinks

- Real Estate (Operations & Services)
- Recreation
- Retail (Grocery & Food)
- Telecom Services
- Telecom (Wireless)
- Utility (General)
- Utility (Water)

Profitability & Growth

Overall, UK SME profitability looks like this:

- Private non-financial corporations' net rate of return was 12.6% in Q3 2018
- The net rate of return for manufacturing companies rose to 15.4% in Q3 2018, up 1.1 percentage points from the previous quarter's net rate of return of 14.3%, after two consecutive periods of decline.
- Services companies' net rate of return was 17.1% in Q3 2018, a decrease of 0.5 percentage points from the revised estimate of 17.6% in Q2 2018[249].

Industries showing many sector-wide profit warnings include Travel & Leisure, General Retailers, and software and computer services.

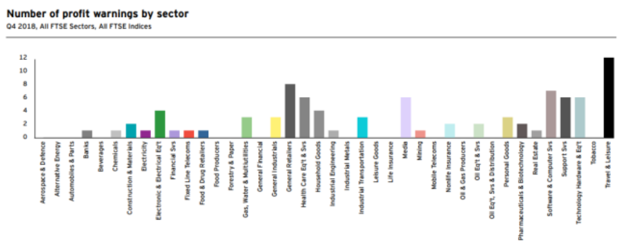


Figure: Profit warnings by sector Q4 2018, EY Profit Warning Dashboard[250]

Of the non-screened out sectors, the ten with highest net margin of Western European publicly traded companies are listed below. Identified priority sectors are coloured green.

Industry	Number of firms in Western Europe	Net Margin
R.E.I.T.	151	66.91%
Real Estate (Operations & Services)	216	54.55%
Banks (Regional)	69	30.21%
Real Estate (General/Diversified)	65	29.01%
Software (Entertainment)	37	22.70%
Bank (Money Centre)	126	21.32%
Investments & Asset Management	327	20.10%
Semiconductor Equip	19	18.96%
Utility (Water)	11	16.97%
Financial Svcs. (Non-bank & Insurance)	123	16.34%

Excluding financial companies results in four more joining the top ten:

Sector	Number of firms in Western Europe	Net Margin
Drugs (Pharmaceutical)	112	15.41%
Semiconductor	31	15.30%
Household Products	73	15.03%
Homebuilding	46	14.30%

The priority sectors themselves are then ranked below according to largest Net Margin.

Industry Name	Number of firms in Western Europe	Net Margin
Real Estate (Operations & Services)	216	54.55%
Banks (Regional)	69	30.21%
Utility (Water)	11	16.97%
Drugs (Pharmaceutical)	112	15.41%
Homebuilding	46	14.30%
Drugs (Biotechnology)	194	11.10%
Healthcare Information and Technology	82	8.16%
Healthcare Products	170	7.97%
Publishing & Newspapers	85	7.95%
Green & Renewable Energy	51	7.43%

[249] ONS Statistical bulletin, Profitability of UK companies: July to September 2018 (18 Jan 2019) https://www.ons.gov.uk/economy/nationalaccounts/uksectoraccounts/bulletins/profitabilityofukcompanies/julytoseptember2018

[250] https://www.ey.com/uk/en/issues/capital-and-transactions/restructuring

From a return on capital point of view, the following are the top ten sectors:

Industry Name	Number of firms in Western Europe	Return On Equity (adjusted for R&D)
Chemical (Basic)	55	38.40%
Software (Entertainment)	37	30.14%
Household Products	73	27.02%
Machinery	208	24.76%
Broadcasting	25	22.84%
Computers/Peripherals	39	21.63%
Air Transport	38	19.94%
Homebuilding	**46**	**19.52%**
Apparel	122	19.28%
Computer Services	217	18.82%

And from the priority SE sector list:

Industry Name	Number of firms in Western Europe	Return On Equity (adjusted for R&D)
Homebuilding	46	19.52%
Publishing & Newspapers	85	15.48%
Real Estate (Operations & Services)	216	14.66%
Healthcare Support Services	42	14.10%
Utility (Water)	11	14.07%
Recreation	54	10.86%
Utility (General)	20	10.58%
Insurance (General)	45	10.07%
Drugs (Pharmaceutical)	112	10.02%
Environmental & Waste Services	48	9.71%

The sectors with the highest expected growth over the next five years as reported by Value Line analysts are:

Industry Name	Number of firms in Western Europe	Expected growth - next 5 years
Reinsurance	4	64.36%
Broadcasting	25	48.88%
Semiconductor Equip	19	41.66%
Education	**10**	**40.35%**
Recreation	**54**	**34.98%**
Drugs (Biotechnology)	**194**	**32.49%**
Green & Renewable Energy	**51**	**32.26%**
Real Estate (Development)	58	31.97%
Computer Services	217	27.46%
Healthcare Support Services	**42**	**27.39%**

And of the priority sectors, their expected growth over the next five years as reported by Value Line analysts, is as follows:

Industry Name	Number of firms in Western Europe	Expected growth - next 5 years
Education	10	40.35%
Recreation	54	34.98%
Drugs (Biotechnology)	194	32.49%
Green & Renewable Energy	51	32.26%
Healthcare Support Services	42	27.39%
Retail (Grocery and Food)	28	23.74%
Telecom (Wireless)	13	20.99%
Homebuilding	46	18.56%
Banks (Regional)	69	17.58%
Farming / Agriculture	43	16.75%

Barriers to Entry

One proxy for high barriers to entry in a particular sector is a high capital expenditure. The sectors in Western Europe with the top ten highest Capex are:

Industry Name	Number of firms	Capital Expenditure (USD)
Power	66	$53,662.34
Telecom. Services	**83**	**$51,685.05**
Auto & Truck	25	$33,253.09
Utility (General)	**20**	**$26,343.12**
Air Transport	38	$19,668.09
Bank (Money Centre)	**126**	**$18,879.28**
Diversified	64	$18,443.64
Drugs (Pharmaceutical)	**112**	**$15,469.17**
Chemical (Specialty)	98	$14,109.03
Auto Parts	55	$13,070.93

Other indicators of high barriers to entry are time to entry, high level of specialist knowledge or expertise required, small number of competitors - highly concentrated markets, economies of scale - only very large competitors, dependent on changing customer behaviour - i.e. switching or high brand loyalty, and unsupportive government policy.

Given these sectors do not generally have lots of social sector representation already, high barriers to entry were considered a disadvantage as social sector organisations were assumed to need to enter these markets.

Buyer & Supplier Power

When it comes to buyer power, at its highest level, and as discussed earlier in this paper, there are four main customer groups each with their own advantages and disadvantages: consumers, government and private and third sector organisations. These are examined in general below.

Source of income	Pros	Cons
B2C	> 'Ethical' and 'social' is trendy > Risk diversified among many buyers, vs one or two large clients > Large brand awareness therefore increased influence & impact through voice > Social media as an opportunity to interact directly with customers	> Heavy (costly) reliance on branding and marketing: getting and holding people's attention is hard > More operational costs to service – higher number of customers per £ turnover > Need to attract many repeat customers > Large and segmented customer base > Often high volume, low margins
B2G	> Secure, low risk counterparty > One large customer > Social Value Act dictates full cost of proposals must be taken into account – should provide competitive advantage for social sector orgs	> Overreliance on a few large commissioners and/or contracts > Large contract sizes make bidding difficult and risky > Harder to sell through red tape – layers of bureaucracy in buying departments > Lower and decreasing margins
B2B	> Often large purchase orders – larger income per transaction > More efficient distribution than direct to customer (B2B2C) > Fewer clients required – less sales need to be won, and can customise products and services to better suit needs	> Smaller market than B2C – less clients > Lower pricing/margins of bulk products than direct > Harder to sell through red tape – layers of bureaucracy in buying departments > Continued business reliance on product or service > B2B2C: Less control of pricing, packaging, placement in store
Third sector	> Shared values as a USP	> Potentially lower volume buyers than B2G or B2B contracts

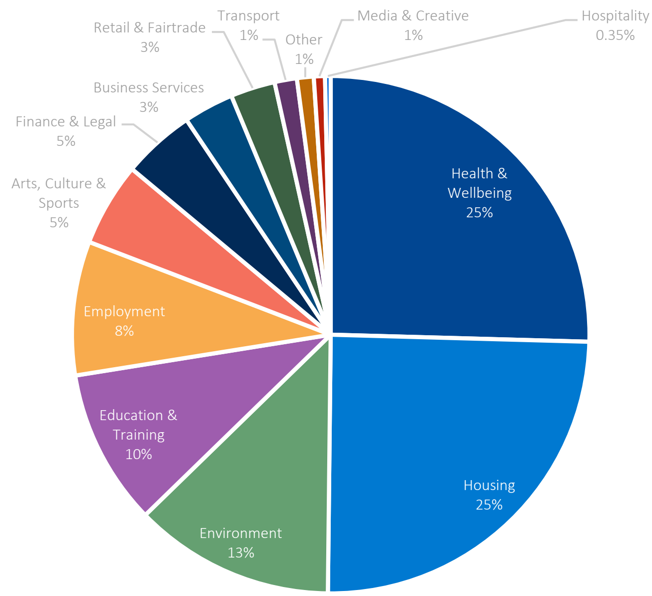
Existing UK social enterprise activity

As this paper is concerned with supporting existing social enterprises to scale rather than supporting new ones to start-up, finding sectors with existing social enterprises at the right stage to grow rapidly is critical to taking a sector-based approach. Here we look at which sectors social enterprises over or under-index, and which sectors could support more social enterprise models.

There are many different sources to find social enterprises in the UK operating at or near to scale. Housing associations, universities, hospices, academy school chains all operate at scale. BSC completed an analysis in 2016 that looked at the following sources: SE100, Social Enterprise Mark, UnLtd's Big Venture Challenge, E3M, the now-closed Technology Spin-out Fund pipeline, and the National Council for Voluntary Organisations (NCVO).

Taking only those with turnover greater than £1m, the most represented sectors are Health & Wellbeing, Housing, Environment, Education & Training, and Employment. Together these make up over 80% of large social enterprises.

Number of UK Social Enterprises by Sector with Turnover > £1m



SEUK's 2017 State of Social Enterprise looks at social enterprises of all sizes, and finds that social enterprises operate across at least 17 sectors in the UK economy. Over half of existing social enterprises work in Health & Social care (16% when combined), Retail (16%), Business support/consultancy (13%) and Education (11%). For the first time since SEUK began doing this survey, Retail is the most represented sector (on its own). They believe this may indicate a trend towards diversification of income, away from the public sector.

SEUK's State of Social Enterprise Survey also asks survey respondents to name social and environmental objectives. The top four are: improving their local community (38%), supporting vulnerable people (30%), improving health and wellbeing (27%) and creating employment opportunities (27%), three of which are cross-cutting impact themes which can apply to business models in many sectors.

Some of these impact areas are sector-specific, like Improving Health and Well-being (27%), Promoting Education and Literacy (17%), and Providing Affordable Housing (4%), where the impact matches a certain industry or sector. This mission-alignment highlights priority sectors where social enterprises could punch above their weight and play a larger, more critical role.

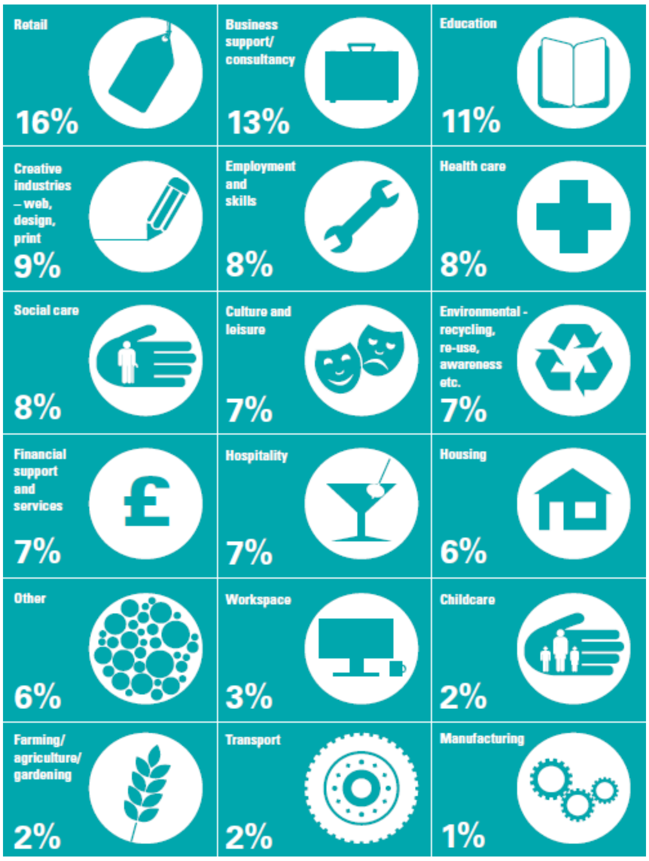


Figure: Principal Trading Activity of Social Enterprises (SEUK State of Social Enterprise 2017)

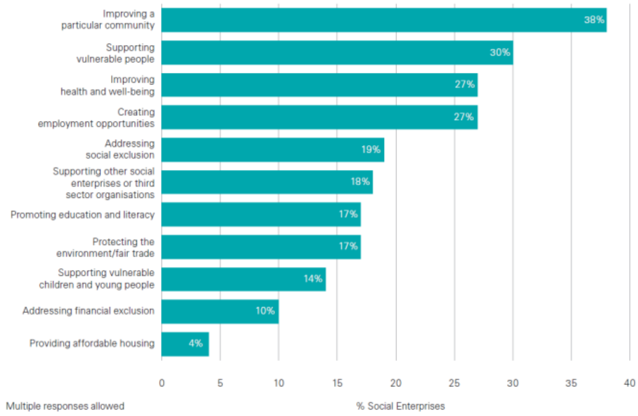
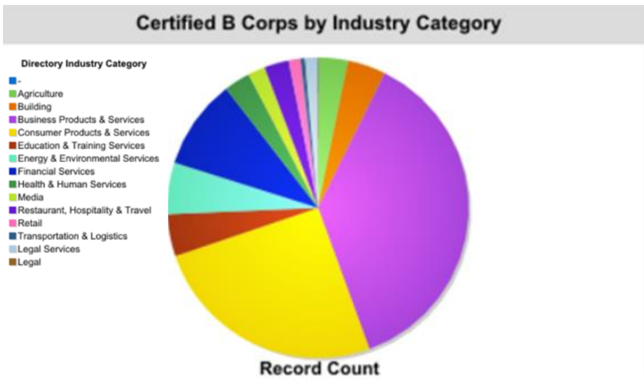


Figure: SEUK State of Social Enterprise Survey - Social and Environmental Objectives

Membership data from Impact Hub King's Cross presents a similar but more nuanced picture, as represented in the figure below. In their 2017 impact report, they state that 97% of their members are working on Sustainable Development Goals, with 28% working on Health and wellbeing and 24% working on education.

Figure: The five SDGs that matter most to the Impact Hub King's Cross community.

B Corps global data shows business and consumer products and services to be by far the largest category represented by their members, followed by financial services.

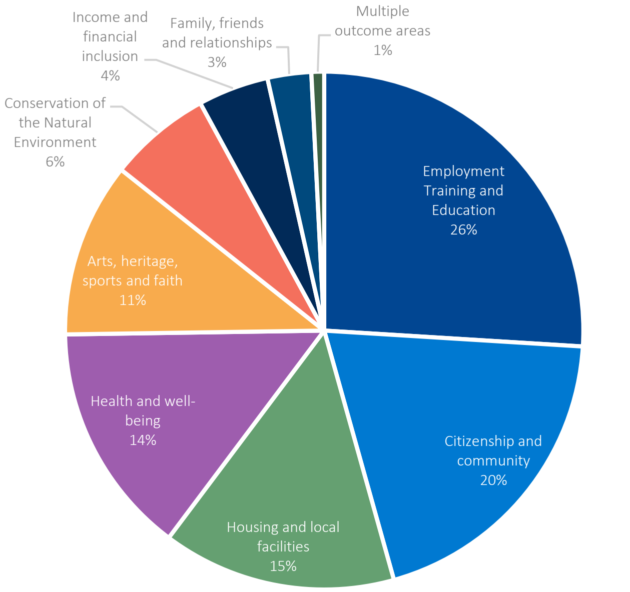


[251]

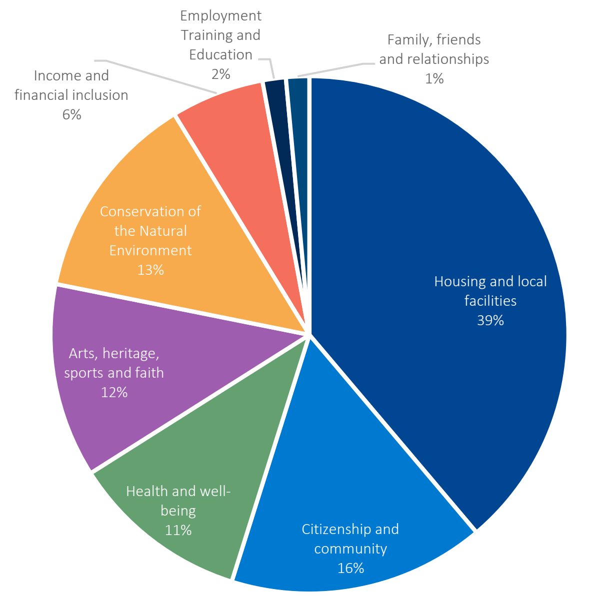
[251] Slides from Katie Hill, Executive Director at B Lab Europe, 13th April 2019

Finally, using raw data from BSC's June 2018 release of its "Deal Level Data", which is a list of social investments into charities and social enterprises both through BSC's portfolio and by other social investors, impact outcome areas can be analysed. Again, the largest sectors include Employment, Training & Education; Citizenship & Community; Housing and Health & Wellbeing.

Outcome Area from BSC Deal-level data by number of deals

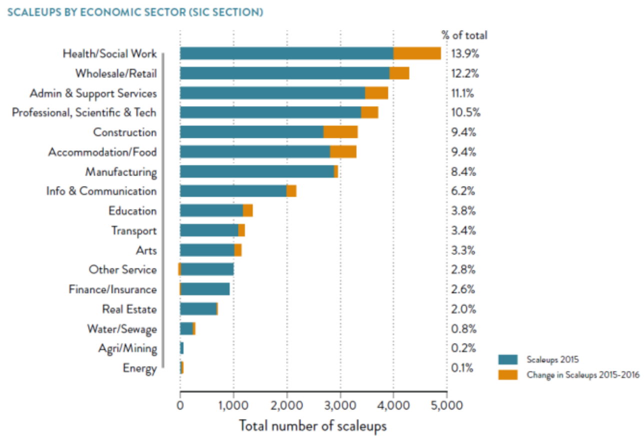


Outcome Area from BSC Deal-level data by number of deals over £1,000,000



High growth companies in private markets

In the private sector, Health & Social Care again is the number one sector for scaleups, according to the ScaleUp Institute Annual Review 2018. In fact, the top six sectors (health & social care, Wholesale/retail, admin & support services, professional services, construction, and accommodation and food) make up 82% of the growth in the number of scaleups in 2016.[252]



Beauhurst tracks a cohort of 1,155 start-up companies that raised equity finance in 2011 in its research: 'Start-ups of yesteryear[253]'. By March 2018, 18% of the businesses have exited, of which 25 businesses, strongly tech-based with just under half operating in the life sciences sector, have been floated on public markets.

It does however, find life sciences and environmental technology (CleanTech) to be particularly risky – the ten companies who raised the most capital before going under were split between these two sectors. In CleanTech in particular, 28% of those that received investment in 2011 have now failed outright, versus 5% of financial firms having failed and 21% exited. Data from the 2017 analysis reveals the following sector breakdown:

Exits and Failures from 2011 Cohort, Selected Sectors

Dead		Exited
9%	Business & Professional Services	14%
14%	Industrials	7%
12%	Leisure & Entertainment	10%
21%	Media	12%
12%	Technology/IP-based Businesses	15%

[252] ScaleUp Institute: Annual ScaleUp Review 2018 http://www.scaleupinstitute.org.uk/scaleup-review-2018/

[253] https://about.beauhurst.com/blog/startups-yesteryear-1/ & https://about.beauhurst.com/blog/startups-of-yesteryear-revisited/