

THE SOCIAL ENTERPRISE INVESTMENT FUND (SEIF) EVALUATION

The landscape of social investment in the UK

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Contents

Introduction.....	2
The nature of social investment	3
The structure of the social investment market	4
Supply-side investors or capital providers	4
Market intermediaries and support services	6
Demand-side or capital users	6
The size of the social investment market	8
The policy context.....	8
Policy chronology.....	9
End notes	12

Introduction

The past twenty years has seen a dramatic change in the definitional boundaries set around the finance sector. As financial services have grown in size and influence in developed economies, the traditional boundaries between ‘economic’ and ‘social’ purpose activities have become increasingly blurred. From a public policy perspective, private finance has been encouraged to play a much more active role in delivering public goods and services with new contractual models such as the Private Finance Initiative blending public and private finance at a project level. Key opportunities for a new type of finance in the UK have included addressing economic exclusion and poverty and supporting community regeneration.

More recently the UK government has also been exploring how better to support outsourcing relationships that go beyond the private sector to include charities and other public benefit organisations including social enterprises. The Social Enterprise Investment Fund (SEIF) within the Department of Health falls within this category. However, whilst the objectives of the SEIF have a clear focus on the fund’s role in improving health outcomes within an expanded – social enterprise driven – mixed economy of frontline health services it is also designed to achieve other impacts. Chief amongst these is a contribution towards the development of the broader social investment sector in the UK sometimes as a finance wholesaler – that builds co-financing deals and structures investment opportunities – and sometimes as a retailer that seeds new social enterprises (including Right to Request start-ups spun out of the NHS) that others can invest in later. The SEIF could, therefore, play an important part in further developing innovation in social investment mechanisms, instruments, and deal structures that may have an influence beyond the health sector alone.

At the outset, it is worth noting that the rationale for the SEIF’s objectives is premised on several contestable assumptions. First, that increasing the flow of finance into health focussed social enterprises will be productive in terms of improved efficiency and effectiveness at the frontline. Second, that these new flows of investment will drive innovation in the sector and that this, in turn, is likely to yield better health outcomes and social returns than further capitalising the status quo. Third, that there is a potential deal pipeline of underserved demand in terms of start-up and growth social enterprises that has the capacity and scope to develop (a market failure argument). Fourth, that there is an appetite for co-investing and co-operations across the institutions of the extant social investment landscape. Finally, in terms of the fund management of the SEIF a further assumption has been made: namely, that the consolidation of the bulk of government capital in social investment in a single organisation – the Social Investment Business (formerly Futurebuilders) – provides the most effective way of building the social investment market. Each of these assumptions will need to be tested during the evaluation of the SEIF’s impacts and effectiveness.

The nature of social investment

Recent work on the social finance landscape in the UK reveals a number of recurring themes that can be grouped under two headings:¹ macro-structural level; micro-market level. Macro-structural level issues focus on the barriers to developing a more coherent account of what social finance is and how it can operate. Emergent themes include:

- Conventional notions of the role of finance and financial markets are increasingly inappropriate for a discussion of social finance.
- Concepts of social finance are blurring the boundaries between private, public, and third sector investment.
- Social finance players operate in a fragmented landscape with little exchange of information or incentives for cooperation.
- There is a lack of financial literacy in social purpose organisations that supports a risk averse approach to new resource strategies. Regulation and legislation is lagging behind trends in social and environmental investment.
- There are limits to the current absorptive capacity of the demand-side.

Micro-market level analyses focus on exploring specific allocative/exchange mechanisms by type of finance. The bulk of the work in the latter has considered how best to approach developing a social finance exchange or stock market.² Emergent themes include:

- Conventional finance markets do not price social or environmental value creation and, consequently, cannot be used to allocate resources to non-profit maximising organisations effectively.
- There is a lack of comparable performance information (metrics) to support the creation of a new or modified social finance marketplace.
- There is a lack of liquidity to support the creation of a new or modified social finance marketplace.
- There is little evidence of strategic segmentation of the investor pool for social finance.
- Conventional finance instruments are underdeveloped or inappropriate for social finance exchanges.
- There is a lack of appropriate capital going towards social finance.

Each of these issues will have relevance to the broader analysis of the SEIF's functions and impacts.

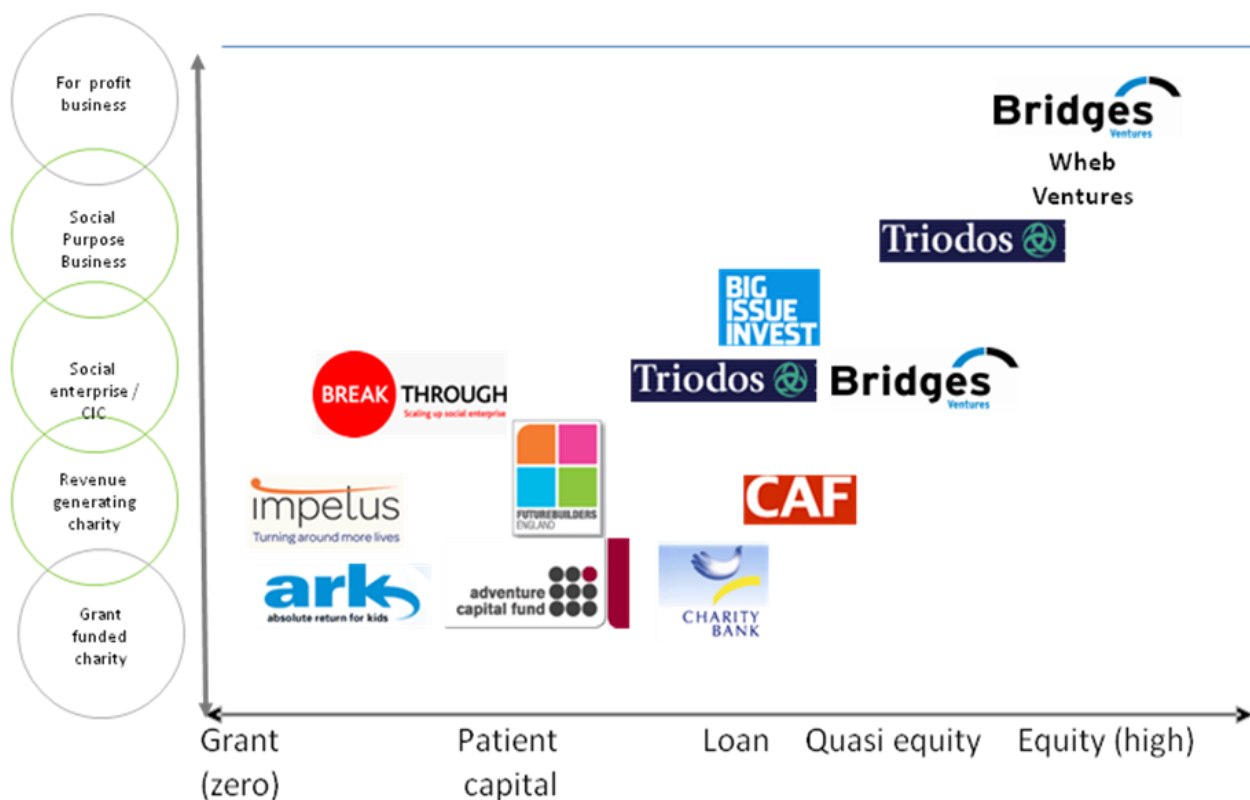
The structure of the social investment market

In terms of structure, the social investment landscape in the UK broadly reflects the structure of conventional capital markets: namely it consists of supply, intermediation, and demand. However, unlike the mainstream markets, government policy has intervened in all three areas of the inchoate social investment market. This is discussed further below.

Supply-side investors or capital providers

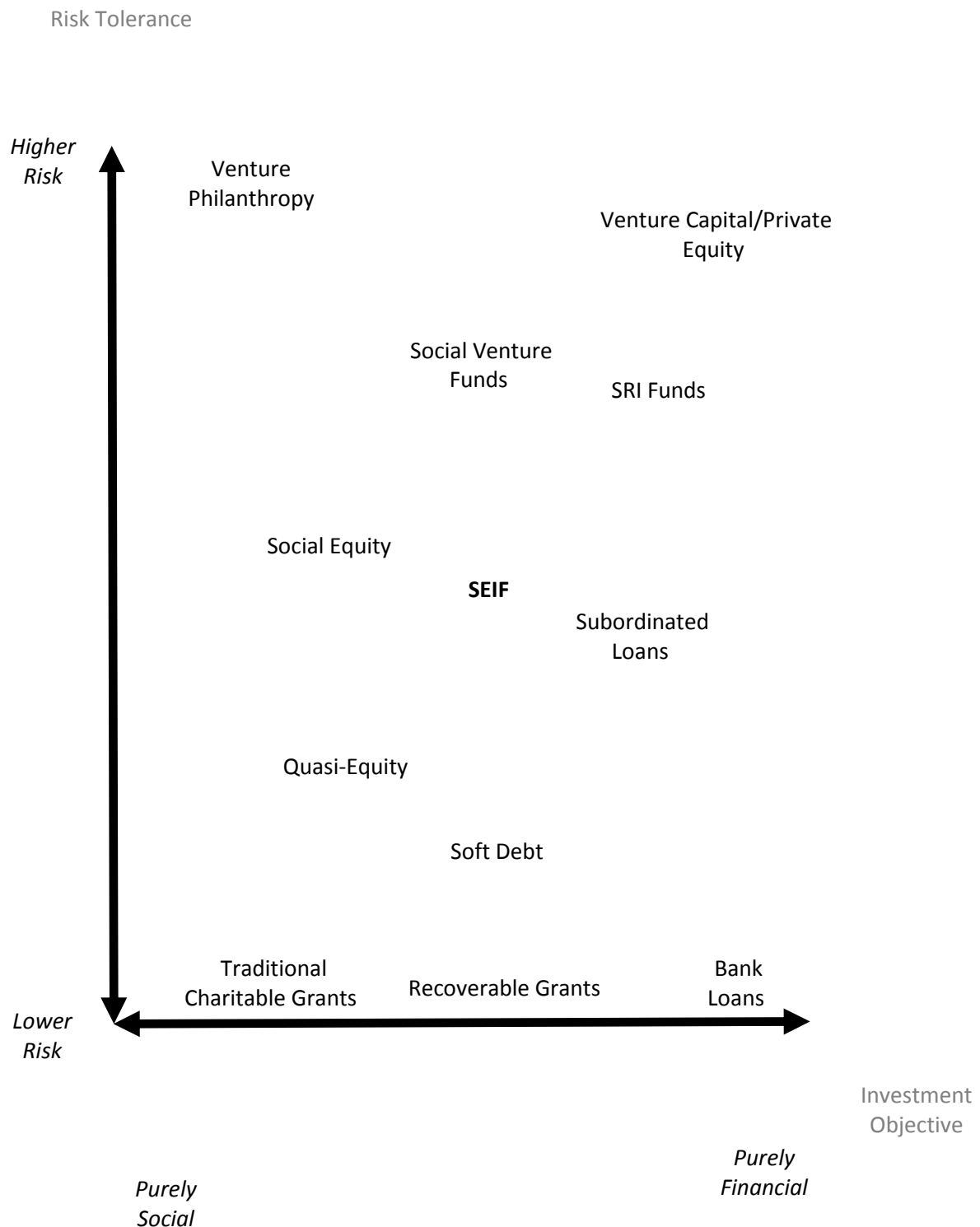
These institutions and individuals provide the funds for social investment typically in the form of either return (debt, quasi-equity) or no return (grants) instruments. The capital providers include: individual or institutional investors along a spectrum of risk-return expectations from market-rate to patient capital; individual or institutional philanthropists, foundations, and charities; public sector grant-givers and procurement contractors; publicly funded venture funds; public sector investment funds. The first category ranges from 'conventional' investors with little interest in social impact who have identified social- or environmental-purpose organisations that offer above market return opportunities to individuals or institutions that aim specifically for social- or environmental-impact investing, even if this produces sub-market returns. Between these two poles lie a range of Blended Value investment models and opportunities. Figure 1 plots the risk-return orientation of some of the key capital providers in the UK against the types of finance they provide. It would appear that the SEIF, potentially, aims to offer finance in competition (or collaboration) with all the organisations represented here.

Figure 1: Supply-side organisations (SITF, 2010)



A second representation of the supply-side of the social investment market categorises type of investment along the two dimensions of risk tolerance (high-low) and investment objective (purely social-purely financial: see Figure 2). In this figure the SEIF sits somewhere in the middle, promising a social impact focus whilst also aiming to recycle some of its investments.

Figure 2: Supply-side investments categorised by risk and objective



Market intermediaries and support services

These are either the financial intermediaries or wholesalers, which act as middlemen between the capital providers and ultimate capital users, or the advisory institutions that provide consultancy services to the investors in this market (see Table 1). In addition to specialised social investment finance institutions (e.g. Charity Bank), there is also an increasing interest in social investment from mainstream financial institutions such as investment banks. For example, in the USA, Morgan Stanley has worked with Blue Orchard to launch the first public collateralised debt obligation of loans to microfinance institutions. The state is an important player in the UK: outsourcing the investment of public money via quasi-independent intermediary organisations such as the Futurebuilders and Bridges Community Investment Fund. Support services in this space include management consultancies (McKinsey's non-profit arm), sector specific research groups (New Philanthropy Capital), legal services (Bates, Wells, and Braithwaite), and bespoke social investment banks (Triodos, Brewin Dolphin).

Table 1: Social investment intermediaries

Intermediary services	Examples of providers
Banking	CDFIs, Credit Unions, Charity Bank, Triodos
Information on Investors	EIRIS
Wholesalers	Social Finance
Sector Information and Research	GuideStar, New Philanthropy Capital
Exchange Platforms	Kiva, Investing For Good, ClearlySo
Donor Advice	Rockefeller Philanthropy Advisors, WISE
Brokerage	Ethex, Aim, Plus Markets Group, IIX Asia
Private Client Investment Management	Geneva Global, GEXSI, IJ Group
Venture Philanthropy Funds	ARK, Venturesome, NESsT, Impetus Trust, New Profit Inc
Social Enterprise Funds	Social Investment Business/Futurebuilders, ClearlySo
Social Venture Funds	Bridges Community Ventures, , Big Invest

Demand-side or capital users

These are the social purpose organisations that are either start-ups or are at a point of investment readiness for growth. Capital users include not-for-profit charities, for-profit social enterprises, community development financial institutions, co-operatives (IPs), and Community Interest Companies. Data suggests that the absorptive capacity of the demandside may be limited: SEC (2009) suggested that the average turn-over for a UK social enterprise was only £2.1 million with only a very small number of organizations generating revenue above £100 million per annum.

An alternative view of the supply-side/intermediary structure of the market would be to separate wholesale and retail sources of funds, namely those that flow from institutional or individual sources. In this model, many of the intermediaries can be seen as wholesalers of social investment. This was the

specific role identified by the UK's former Labour government for a new wholesale bank that would distribute unclaimed assets from retail banks to youth and social projects (Commission on Unclaimed Assets, 2006). This project has now been renamed as the Big Society Bank by the Coalition government formed in May 2010.

A fourth group of players in the landscape are driving new collaborations and, particularly, new knowledge exchange to build the supply-side of social investment. Not all the players in this emerging field are aware of all the others nor, where they are, is good communication over market building. This is especially true for the investors across the different categories of social investment. Many of these initiatives aim to increase market transparency, enhance communication, build greater interaction within and between investor groups, and increase the accessibility of funds for the interested parties. Some of these provide each group of investors with online environments where they can interact, share information, and experience. There are also numerous research initiatives. Some focus on specific questions and issues, like building a social equity market, whilst some are interested in broader research on social investment issues.

Tables 2-4 provide summaries of the structure of the social investment market in the UK with example organisations.

Table 2: Supplyside Investors

The State	Department of Health
Members of Co-operatives	Baywind local communities
Philanthropists	Tom Hunter
Foundations	Gates Foundation
Ethical Investors	Friends of cafedirect
Venture Philanthropists	Permira
Commercial Investors	Sainsbury family

Table 3: Intermediary Wholesale Institutions

Credit Unions/Mutual Funds/Cooperatives	Nationwide Building Society
Microfinance Institutions	SKS
Stock Markets/Platforms	Impact Investing Exchange Asia
CDFIs	London Rebuilding Society
Investment Banks	Investing for Good
Venture Philanthropy Funds	Impetus Trust
Government Brokers	Social Investment Business
Advisory Services	New Philanthropy Capital

Table 4: Demandside Investees

Charities	St Giles Trust
Community Interest Companies	Hackney Community Transport
Co-ops	Mondragon
Micro-entrepreneurs	Kiva investees
Not-For-Profit Social Entrepreneurs	Apopo
Green Technology Entrepreneurs	Memset
For-Profit Social Entrepreneurs	Ethical Property Company
Commercial Businesses	cafedirect

The size of the social investment market

The amount of capital currently present in the social investment market is difficult to calculate exactly. This is largely because of two factors: the wide variety of types of capital and investment mechanisms present in this space (from grants to full market return equity); the absence of a unified market or exchange platform for social investment. However, a rough calculation can be made based on the following: social equity investment (i.e. share issues in UK social enterprises) (£50.1 million);³ the assets of co-operatives (£8.5 billion);⁴ the annual turnover of social enterprises (£27 billion);⁵ the annual turnover of co-operatives (£27.4 billion);⁶ the assets held by venture funds aiming at social impact (£32 million);⁷ the assets held by social enterprise venture funds (£15.5 million);⁸ the assets held by venture philanthropy funds (£10 million);⁹ government procurement contracts to charities (£23 billion);¹⁰ the ethical consumption market (£29.3 billion);¹¹ UK government funds committed to social investment (£572 million).¹² This gives a total figure of approximately £116 billion.

Two further sources of capital may also be taken into account. The proposed establishment of a social investment wholesale bank capitalised by the dormant, unclaimed, assets held by UK banks would provide an additional source of social investment capital that is estimated to be worth in excess of £400 million.¹³ Finally, it could also be argued that it is appropriate to include 'core' SRI assets under management in the UK as part of the social investment market. If so, this would more than triple the figure above by adding in an additional £500 billion.¹⁴

In terms of the sizes of deals being made within the social investment market, there is a concentration on smaller investments typically up to £250,000 across a range of grant, debt and quasi-equity (grant availability is particularly concentrated up to around £50,000). Larger investments tend to be debt and there are relatively few deals in excess of £500,000. There is some evidence that suggests that this is the consequence of demand-side issues rather than a lack of investment capital.¹⁵

The policy context

Since 1997, the New Labour government has been a world-leader in pursuing a range of policy agendas and interventions to facilitate the development of the social investment market. It has particularly focussed on new forms of social investment that support innovation in meeting priority public needs. The government has consulted widely as part of the policy process and, as a consequence, has had to wrestle with many competing conceptualisations and priorities for social investment across civil society. This has also had the effect that policy formation has, at times, been reactive and implementation fragmented across a variety of government departments with forms of social investment not necessarily recognised as such.

Social investment policy in the UK has developed in three interrelated and broadly sequential stages (see Table 5). The first involved direct funding of intermediaries and an engagement with mainstream capital that aimed to address access to finance issues for businesses and community and social enterprises in disadvantaged areas. There were a range of drivers behind this stage, notably: 'community investment' policy in the USA; private sector initiatives around improved corporate

citizenship and corporate social responsibility; civil society innovations aimed at addressing macro-level investment market failures and promoting micro-level 'bottom-up' forms of community regeneration.

The second stage focused on investment to enable the development of the social enterprise sector, especially in the context of building the capacity of third sector organisations to deliver public services in a wider mixed economy of welfare. Many of the models of welfare provision that emerged operated in quasi-markets and took the form of hybrid organisations that combined (or partnered with) private, public and civil society logics and business models. A, perhaps, unintended consequence of this move toward greater hybridity and sectoral blurring has been a change to the nature of some markets themselves.

The third, and most recent, stage emerged with the discussions around a Social Investment Wholesale Bank (SIWB) in 2006. This initiative was the product of the Commission on Unclaimed Assets (2006) that proposed the use of deposits in banks and building societies that had not been accessed for a significant amount of time, to finance a Social Investment Bank (SIB).¹⁶ In 2008, the UK Government published the Dormant Bank and Building Society Accounts Act 2008 to enable the use of such money for public purposes, including a potential SIB. The consultation for the SIB suggested that it would better function as a wholesaler of finance that aims to increase the size and scope of the social investment market rather than act as a retailer investor itself. This would be achieved by using structured finance (for example guarantees) to leverage significant mainstream capital into social investment. The proponents of the SIWB envisaged a step-change in both the amount, variability and appropriateness of the social investment market as a result of this government-initiated intervention. This approach also marked a shift in government strategy, since it was more focused on leverage and brokerage rather than direct fund creation by government. In 2009, the new Coalition Government confirmed its commitment to this project, but under the new title of the Big Society Bank (see above).¹⁷

Table 5: The development of UK social investment policy

Stage One	Social investment as 'community investment'	1999 onwards
Stage Two	Social investment in third sector organisations, particularly social enterprises.	2001 onwards
Stage Three	Social investment as a way to realise (combined) social, environmental and economic outcomes.	2009 onwards

Policy chronology

In 1999, the Social Exclusion Unit was established within the Cabinet Office. A key focus was to improve access to finance in disadvantaged areas to support new economic activity such as start-ups, particularly through new or enhanced Community Development Finance Institutions (CDFIs). Thus,

social investment policy began with an agenda to accelerate community investment in geographical areas of deprivation where there was a market failure in terms of access to mainstream finance.

To build on these initiatives, in 2000, the government established a Social Investment Task Force to focus on further improving access to finance in disadvantaged areas.¹⁸ The Taskforce's remit was 'to set out how entrepreneurial practices can be applied to obtain higher social and financial returns from social investment, to harness new talents and skills to address economic regeneration and to unleash new sources of private and institutional investment. In addition, the Task Force should explore innovative roles that the voluntary sector, businesses and Government could play as partners in this area' (SITF, 2010). The recommendations of the Social Investment Task Force led to a range of government policies including:

- a Community Investment Tax Credit (implemented in 2002 as the Community Investment Tax Relief);
- a Community Development Venture Fund (Bridges Community Ventures Ltd was set up in 2002 as the first community development venture company with investment from government as well as the private sector);
- greater latitude for investment in community development initiatives by charitable trusts and foundations (the Charity Commission partly enabled the development in the UK of programme related investment or PRI);
- support for Community Development Finance Institutions (a Community Development Finance Association was set up as the trade body for CDFIs in 2002, part-funded by the UK Government).¹⁹

The work of the Taskforce also led to the launch of the Phoenix Fund in 2000 which included three elements: a development fund supporting business and social enterprise start-ups and support in disadvantaged areas and for disadvantaged groups; a challenge fund and loan guarantees for CDFIs (2003); and a national network of volunteer business mentors.²⁰ The development fund was, in effect, a risk fund and thus a new way for government to intervene.

In 2001, a Social Enterprise Unit was set up in the then Department of Trade and Industry (now part of Business Innovation and Skills). It specifically considered access to finance (both working and investment capital) as well as new organisational structures. One of its first acts was to consult on and develop legislation for a new business form for social enterprises, the Community Interest Company (CIC). The CIC was launched in 2005. The CIC has an asset lock, is subject to a community interest test, can pay shares under capped conditions and can either be set up as a company limited by guarantee or by shares. By January 2011, over 4500 CICs have been registered, though there is little evidence yet that this has resulted in any significant new social investment despite recent reviews of the dividend and interest caps required of this legal form

Next, in 2002, the Government funded the Adventure Capital Fund (ACF) to be delivered by third sector organisations. It was set up in order to develop capacity and increase the impact of medium-sized community organisations through the development of either physical assets or social enterprise

activity and experimented with mixes of support, grant, patient loan and forms of equity. The funded was capitalised with £14.4m government funding.²¹

At the same time, trends within voluntary and community sector organisations, and the environment within which they worked, (particularly the increase in market contracts for public service delivery) were leading to more interest in, and need for, appropriate investment.²² Concern over the suggested undercapitalisation and fragility amongst such organisations led different parts of the third sector and government to address the nature and flows of finance into the sector. Part of the government's response was to create Futurebuilders, building on the model of the ACF, that aimed at capacity-building third sector organisations primarily to deliver public services.²³

In 2006, the UK Government brought together the Social Enterprise Unit with voluntary and community sector government functions, under the Office of the Third Sector (OTS) within the Cabinet Office. The OTS described 'social investment' as 'investment made for a social purpose in organisations committed to delivering benefits [to] society and the environment. This investment – whether from grants, loans, equity investments or other emerging forms – can enable third sector organisations, including social enterprises, to develop their operations and become more sustainable'.²⁴ The OTS developed a range of initiatives designed to enable the expansion of the social investment market across supply, intermediation and demand (see Table 6).

Table 6: Government sponsored social investment policy initiatives 2004-2009

Supply	Intermediation	Demand
Adventure Capital Fund	Social Return on Investment (SROI) Review	Research: Third Sector Research Centre (Birmingham/Southampton)
Futurebuilders	Social Investment Almanack	Capacity Building: in tandem with Regional Development Agencies and Business Links
Community Builders	Sponsorship of Good Deals Conference	Financial Awareness: OTS-NESTA (Social Enterprise Access to Investment programme)
OTS Risk Capital Fund	Action Research Pilots (with Community Innovation UK and Charity Bank)	
	NESTA review of tax incentives for social investment	

Various other government departments – including Health – developed their own social investment policy initiatives during this period. For example, in 2008, the Department for Children, Schools and Families launched a £100m Youth Sector Development Fund that promoted and supported growth and capacity in third sector organisations that deliver effective services and activities for young people in England (particularly the most disadvantaged).²⁵ The Financial Inclusion Taskforce was also established in 2005 within the Treasury. It set up a £120m Financial Inclusion Fund that included a £36m Growth Fund to support credit unions and social lending in disadvantaged areas.²⁶ In 2009, the

Department for Communities and Local Government set up and funded a new Asset Transfer Unit to support community building with the transfer of public assets.²⁷

The new Coalition Government has demonstrated a commitment to a number of the previous government's policy initiatives in social investment. These include the continuation of the £100 million Social Enterprise Investment Fund within the Department of Health (administered by the Social Investment Business), further support for the Social Impact Bond initiative developed by Social Finance, as well as the Big Society Bank, drawing on unclaimed assets within the major retail banks. However, it is already clear that the policy frameworks within which these projects are set will be very different from what went before and it is, therefore, likely that a new set of state objectives for social investment will emerge during this government's lifetime. At the same time, calls for a reduced state involvement in social investment are growing.²⁸ These institutional shifts may well augur a strong private sector turn in the social investment landscape over the next five years. The growth of interest in a range of types of for-profit social investment (often identified as 'Impact Investment') provides some evidence of this (O'Donohoe et al, 2010).

End notes

¹ Nicholls with Pharoah (2007), Emerson and Spitzer (2007)

² There are several references in the literature to the social capital market (Emerson, 2003; Hartzell, 2007). This does not refer to the more common notion of 'social capital' developed by Bourdieu (1986), and later popularised by Putnam (1995). Social capital in the Putnam sense refers to the social networks that are an integral part of social groupings, and has been utilised in research and policy as an indicator of the strength of social and community relationships. Emerson et al (2007), make an interesting distinction between 'integrative' and 'transactional' social capital with the former representing Putnam's definition and the latter referring largely to social finance. Emerson et al (2007) note, however, that the two are linked as part of an 'integrated social capital market of which all human exchange (whether social or financial) is part' (p. 6).

³ Hartzell (2007)

⁴ Co-operative Monitor (2008)

⁵ DTI (2006)

⁶ Co-operative Monitor (2008)

⁷ Bridges Community Ventures Ltd (BCV) manages two venture funds totalling £52 million of assets. The funds provide investment specifically for small businesses in deprived areas and include £20 million in government matching investment

⁸ Bridges Social Entrepreneurs Fund worth £8.5 million; Big Invest Fund worth £3 million (incomplete); Triodos Social Enterprise Fund worth £4 million

⁹ The two largest VP funds in UK – Impetus Trust and the CAN/Permira Breakthrough Fund – total £7.1 million in investments to date

¹⁰ NCVO (2008)

¹¹ Nicholls (2007)

¹² This figure is the total of: UnLtd funded by £100 million of public money from the Millennium Fund; Futurebuilders funds worth £250 million which offers investment packages of grants/loans/technical for highly selected organisations with reasonable prospects of winning service-delivery contracts; Community Builders grant fund worth £70 million; the Adventure Capital Fund worth £12 million, that offers longer-term financial and development investment to support enterprise growth; a £20 million challenge fund for social enterprise in recognition of the need to stimulate growth; a Community Asset Transfer fund of £30 million to support local authority asset transfers into community ownership; the SEIF with funds of up to £100 million

¹³ Mathiason (2007)

¹⁴ Eurosif (2008) identified two categories of SRI investment:

- Core SRI: elaborated screening strategies impacting portfolio construction and implying a values-based approach. Investments are characterised by ethical exclusions (more than two negative criteria) as well as different types of positive screening (e.g. best in class)
- Broad SRI: mainstreaming of SRI reflecting the growing interest in this area by institutional investors. Investments are characterised by simple exclusions, engagement and integration of environmental, social and governance risks (ESG) into conventional financial analysis

¹⁵ Bank of England (2003); TSO (2008)

¹⁶ www.unclaimedassets.org.uk/downloads/CUA_report_FINAL.pdf

¹⁷ See: <http://www.cabinetoffice.gov.uk/content/big-society-overview>

¹⁸ The Social Investment Task Force was an initiative of the UK Social Investment Forum, in partnership with the New Economics Foundation and the Development Trusts Association.

¹⁹ www.cdfa.org.uk

²⁰ www.berr.gov.uk/whatwedo/enterprise/enterprisesmes/building-enterprise/enterprising-people/Phoenix%20Fund/page37783.html

²¹ www.adventurecapitalfund.org.uk

²² These trends included reductions in grants, increased contract opportunities from the public sector, shifts from grants to contracts by government, a decline in giving for some organisations and an increase in earned income strategies.

²³ www.futurebuilders-england.org.uk

²⁴ www.cabinetoffice.gov.uk/third_sector.aspx

²⁵ www.ysdf.ecotec.com

²⁶ www.financialinclusion-taskforce.org.uk/

²⁷ The Assets Transfer Unit is being run by the Development Trusts Association (DTA), Community Matters and the Local Government Association www.atu.org.uk

²⁸ For example: <http://www.socialedge.org/discussions/responsibility/social-enterprise-and-the-death-of-the-welfare-state#1296249997>

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