The Ubele Initiative

Is Loan Finance Right for Your Charity or Social Enterprise?

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Introduction

If you're exploring the world of loan finance and its suitability for your charity or social enterprise, understanding the many nuances of this funding avenue is key. There are advantages, opportunities and challenges to consider specific to charities and social enterprises, especially those run by teams from Black and Racially Minoritised communities. We took a deep dive into loan finance for charities and social enterprises with the support of Karen Hobson, former Investment Manager at Key Fund. This guide explores the key information you need to know about this funding option and offers insights to help you make an informed decision about the future of your business.

This information does not constitute financial advice or recommendation and should not be considered as such.

Loan Finance in the Wider Funding Landscape

WHAT ARE MY OPTIONS?

Loan finance represents a crucial segment in the landscape of funding options, which includes grants, donations, equity investments, community share offers for cooperatives and crowdfunding. Each of these sources has its own merits and limitations.

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WHY LOANS?

Loans stand out for their ability to provide immediate, larger sums of capital, which is often not possible with grants or donations. They are particularly valuable in situations where timing and the amount of funding are critical to seize growth opportunities or implement large-scale projects.

The Unique Challenges Faced by Black and Racially Minoritised Business Owners

ADDRESSING SOCIETAL BARRIERS

Organisations led by Black and Racially Minoritised Communities can confront unique challenges, such as systemic barriers to accessing capital, biases in lender evaluations, and a lack of representation in financial networks. The recent Reforming Social Enterprise report from the Adebowale Commission highlighted that structural barriers prevent Black-led social enterprises from accessing social investment and debt-based finance. SIB's analysis of data on over 4,000 organisations in its diversity dashboard found that Black and Racially-Minoritised-led organisations tend to be smaller in size and less likely to access loan finance. We developed the Flexible Finance programme to level the playing field and make loan finance more accessible to Black and Racially Minoritised Communities.

Who Can Use Loan Investment?

EMPOWERING COMMUNITIES

All sorts of organisations can benefit from social investment; these might include anything from community-run pubs, swimming pools, libraries, theatres, sports associations, nurseries and local co-operatives, especially those in disadvantaged areas or those overlooked by mainstream banks. The common thread among these investees is a strong ambition to bolster and empower communities (Karen Hobson).

FLEXIBLE FINANCE

The Ubele Initiative's Flexible Finance scheme aims specifically to support organisations that are improving people's lives or the environment they live in with loans of between £50k and £1.5m, up to 100% grant match funding on loans secured, which is an example of blended finance.

Understanding the Basics: Jargon Glossary

When considering loan finance, there's a lot of jargon thrown around that can be difficult to decipher. Grasping the fundamental aspects of financial tools can help with your journey with loan finance. If you need any clarification, email josh.faconerroberts@ubele.com. We are happy to help.

LOAN TERMS AND TYPES:

- **Loan Finance:** Money borrowed that must be repaid, usually with interest.
- **Interest Rates:** The percentage charged on the total amount of borrowed money. These can vary widely. Fixed rates offer predictability in repayments, whereas variable rates can fluctuate with market conditions.
- **Repayment Terms:** The conditions and duration for loan repayment. Short-term loans might be suitable for immediate needs, while long-term loans can be aligned with long-term revenue generation projects.
- **Blended Finance:** Mixing loans with grants to reduce repayment burdens and overall risk.
- **Flexible Finance:** Financing with adaptable repayment terms. It is also the name of the loan scheme run by The Ubele Initiative in partnership with SIB and Access.

FINANCIAL INSTRUMENTS AND CONCEPTS:

- **Grants:** Funds given, usually for a specific purpose, without the need for repayment.
- **Donations:** Gifts given by individuals or organisations without expectation of return.
- **Equity Investments:** Money invested in a company in exchange for shares.
- **Community Shares:** Equity investments in cooperatives offering social returns, mutual benefits and democratic control. More information here.
- **Crowdfunding:** Raising money from many people. It is generally raising small amounts of money from a large number of people, typically online.
- **Peer-to-peer Lending Platforms:** Online platforms where individuals can lend money to others directly.
- **Capital Repayment Holiday:** A period during which a borrower is allowed to pause repayment of the principal amount of a loan.
- **Investment Committee:** A group of individuals responsible for making decisions about investments, often related to managing and allocating funds.
- **Principal Loans:** The initial sum of money borrowed or invested, excluding any interest or dividends.
- **Secured Loan / Unsecured Loan:** A secured loan is backed by collateral, reducing risk for the lender. An unsecured loan does not have collateral, usually carrying higher risk and interest rates.

FINANCIAL ANALYSIS AND PLANNING:

- **Cash Flow:** Total money movement in and out of a business.
- **Debt-to-Income Ratio:** A measure of an individual's monthly debt payments compared to their monthly gross income.
- **Liquidity:** This refers to how quickly and easily assets or investments can be converted into cash without affecting their market price. In business, it's a measure of the ability to meet short-term obligations.
- **Balance Sheets:** Financial statements that provide a snapshot of a company's financial position at a particular time, showing assets, liabilities, and equity.
- **Income Statements:** A financial statement showing the company's revenues and expenses over a specific period, indicating how the revenues are transformed into net income or profit.
- **Cash Flow Analysis:** The study of a company's cash inflows and outflows to evaluate its financial health, particularly its ability to generate cash to meet debts and operating expenses.
- **Budget Forecasts:** Predictions of future income and expenses.
- **Scenario Planning:** The process of envisioning possible future conditions and developing plans to effectively respond to those potential situations, often used in risk management and strategic planning.
- **Risk Assessment:** The identification and analysis of potential issues that could negatively impact key business initiatives or projects.
- **Contingency Plans:** Prepared strategies or actions designed to help organisations respond effectively to potential future events or situations.
- **Reserve Funds:** Funds set aside for future needs or emergencies.
- **Revenue Streams:** Sources of incoming money for a business.
- **Capital Investment:** Funds invested for business objectives.
- **Governance:** Rules and processes directing a company.
- **Financial Health:** The state of a company's finances.
- **Financial Viability:** Savings or funds set aside by an organisation to cover future liabilities, emergencies, or unforeseen costs.

MANAGEMENT AND STRATEGY:

- **Partnership Manager:** A professional responsible for managing relationships and collaborations with other organisations or stakeholders.
- **Senior Leadership Team:** Management responsible for strategic decisions.
- **Turnover:** The total revenue generated during a specified period.
- **Impact Strategy:** A plan or approach detailing how an organisation intends to achieve its social or environmental goals.
- **Impact Metrics/KPIs:** Quantitative measures used to assess the effectiveness of an organisation in achieving its objectives.
- **Sustainability:** The ability to maintain or support an activity or process over the long term.
- **Social Impact:** The effect of an organisation's actions on the well-being of the community and environment.
- **Non-repayable Component:** In the context of blended finance, it refers to the grant portion of the financing, which does not need to be repaid.
- **Structural Barriers:** Systemic impediments that make it harder for certain groups to access services or opportunities.

When Are Loans a Suitable Option?

It's important to know the best time to consider a loan for your business. Loans have their own benefits compared to other funding options like grants and donations. Here are some situations where a loan can be particularly beneficial:

CONSISTENT INCOME

If your business regularly brings in money, using a loan can be a suitable financial move.

EXPANDING YOUR BUSINESS

When you're looking to scale your operations, or replicate your business model in new areas or communities, a loan can give you the financial boost needed for this expansion.

NEED FOR MAJOR PURCHASES

Loans can be helpful when you need to invest in significant assets or infrastructure that will benefit your business in the long run, like new equipment or facilities.

FILLING TEMPORARY FINANCIAL GAPS

If you're waiting for confirmed funding from grants or other sources, a loan can provide the necessary funds in the interim.

Pros and Cons of Social Loans

The advantages of loan finance are accessibility, as it can be tailored for organisations traditionally excluded from mainstream financial systems, and flexibility, as it can cover various needs from equipment purchase to property renovation, and the grant element, as providing a non-repayable component eases the financial burden. Disadvantages include repayment obligation, unlike grants, a significant portion needs to be repaid, and financial discipline, as social investment requires rigorous management of finances to meet repayment schedules (Karen Hobson). Some other elements to consider include:

PROS

- Timely access to funds: Loans can be arranged relatively quickly compared to grants.
- Building Credibility: Receiving a loan can help maintain the credibility of the organisation in the long term with other potential investors.
- Strategic growth and development: Loans can enable strategic investments in growth or development that other funding types may not support.

CONS

- Potential for financial strain: Misaligned or overly optimistic revenue projections can lead to financial difficulties.
- Risk to assets: For secured loans, your assets are at risk if you are unable to make the loan repayments.
- Cost: loans must be repaid with interest. This means that taking on a loan often comes with additional costs.

The Class Model is a framework to use when deciding whether to pursue loan finance. (Credit: Karen Hobson)

C

Capacity – Do you have the capacity to take on the investment and manage the money well? Have you got the right team (is it volunteer-led or staff-led)? Do you have robust financial management systems and social impact collection methods?

L

Legal Structure – Does your governing document allow you to borrow funds? It's important to check.

A

Aptitude – Have you got a knowledgeable team, with a clear plan of how the funds will be used and managed?

S

Sellable product or Service – Do you have a sellable product or service that will enable you to repay any investment secured?

S

Sustainability and Support – Do you have a clear sustainability plan, and how will an investment support this process? Is your Board on board to support the process of acquiring social investment and fully understand what is involved?

How Investors Assess Loan Applications

When charities and social enterprises apply for loans, investors look at their applications from many angles. It's not just about whether the business can pay back the loan. They also consider how the business impacts society and if it can manage the loan well. To improve your chances of getting a loan, it's important to understand what investors are looking for.

However, it's important to remember that a relational approach is often used, where lenders engage closely with organisations to understand their specific needs, challenges, and objectives, ensuring that a loan investment aligns well with the organisation's overall mission and context. It may seem intimidating to have someone scrutinising your business, but the lender wants to support your business and make sure that the outcome is mutually beneficial.

MAKING A STRONG APPLICATION

- Have a clear and realistic business plan that explains how your business will have a positive social effect.
- Show good management and a reliable plan for your business' finances.
- Clearly state your business goals, how you'll make money, and what you need the loan for.

FINANCIAL HEALTH

- **Current financial status:** Investors check your balance sheets and income statements to see if your business is financially stable right now. They also look at your cash flow to see how well you manage day-to-day money and compare your debt to your income to understand your existing financial responsibilities.
- **Future plans:** They want to see detailed predictions of your future budget to understand where your business is heading financially. They also look at how well you've planned for different future scenarios and how realistic your assumptions are.

SOCIAL IMPACT

- **Impact strategy:** Have clear goals for how you want to make a difference socially or environmentally.
- **Impact metrics:** Have data available to show the social impact you're making.
- **Alignment with mission:** Make sure your plan for using the loan matches your business' main goals.

LONG-TERM PLANS

- **Community engagement:** Show how your project will help the community over the long term.
- **Scalability of impact:** Demonstrate the potential to expand or repeat your project's positive effects elsewhere.

GOVERNANCE AND TEAM

- **Leadership team expertise:** Highlight the range of skills and experience within your leadership team. This includes expertise in finance, management, the specific sector you work in, and any other relevant areas. Investors look for a team that can effectively steer the organisation towards its goals.
- **Team dynamics and capacity:** Demonstrate that your team works well together and has the capacity to deliver the proposed work. Show how your team's structure and dynamics contribute to achieving your business objectives and managing the loan.
- **Decision-making processes:** Explain how decisions are made within your organisation. This includes outlining the roles and responsibilities of different team members and how they contribute to strategic decisions, especially those related to finance and project management.
- **Stakeholder involvement:** Discuss how you involve stakeholders (like beneficiaries, community members, employees, and volunteers) in your governance and decision-making processes. This shows investors that your team is connected to the needs and feedback of those you serve.
- **Training and development:** Describe any training and development opportunities you provide to your team. This demonstrates a commitment to continuous improvement and adapting to changing needs and challenges.
- **Succession planning:** Outline your plans for leadership succession to ensure long-term stability and sustainability. This reassures investors about the future of your organisation beyond the current team.

ABILITY TO REPAY THE LOAN

- **Past repayments**: Show that you've successfully repaid loans or debts before.
- **Stable income:** Prove that your business consistently makes enough money to meet loan payments.
- Plan for risks:
- **Risk assessment:** Evaluate all risks related to repaying the loan and have mitigation and contingency plans in place.
- **Reserve funds:** Have extra funds set aside for making loan payments in tough financial times.

Finding Loan Opportunities

- Specialised lenders: Some lenders focus specifically on social enterprises and charities, offering more tailored and flexible loan products.
- Government-backed schemes: These can offer favourable terms, especially for organisations in the social sector.
- Peer-to-peer lending platforms: These platforms can offer an alternative to traditional bank loans, often with less stringent requirements.

You can find a list of UK social investors, funds and advisers in the Good Finance Directory.

Flexible Finance

The Ubele Initiative's partnership with the Social Investment Business (SIB) and Access – the Foundation for Social Investment is making loans more accessible for charities and social enterprises led by people from Black and Racially Minoritised communities. In addition to a loan, organisations receive:

- Personalised support to apply for Flexible Finance
- Unrestricted grants of up to 100% of the loan value (capped at £200k)
- Bespoke business support once finance has been secured

To be eligible to apply for Flexible Finance and receive additional support as a Black and Racially-Minoritised-led organisation, the following criteria apply:

- Charity or social enterprise
- At least 51% of Board and Senior Leadership Team from Black and Racially-Minoritised-led communities
- Above £200k turnover
- Applying for a loan of between £50k and £1.5m
- Operating for more than 2 years
- Operating in England

For more information, contact josh.falconerroberts@ubele.org, or arrange a call to discuss your organisation and your plans by completing this form. All details on Flexible Finance, including full eligibility criteria, FAQs and application form can be found here.