The Gritty Reality of Social Investment: when is it the right time for a charity to take on loan finance?

By | A Social Investor
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Charities are often reluctant to take on loan finance, preferring instead to rely on grants from trusts or individuals.

That’s understandable, but sometimes a loan is the best way of bridging a cashflow gap or securing capital to invest in an organisation’s future. As a funding body specialising in the social sector, we find we’re often approached only after traditional fundraising avenues have failed or fallen short. This means many charities are unprepared for the loan application process and haven’t factored it into their plans.
How it happens

We received an application from an independent leisure charity in the middle of raising funds to develop their site and improve the visitor experience. Almost 60% of the necessary funds had been secured from a sports fund, but the charity’s trustees were aware that they would only receive the grant once the work was complete and invoices received. This situation is unfortunately common within the sector, as grants are often paid at the end of a project, rather than at the beginning when they are usually needed.

Like many other charities, the organisation’s first thought was to secure an overdraft that could see them through their cashflow problem. However, negotiations with their high street bank fell at the first hurdle.

Where to go

Fortunately, one of the trustees had a connection to a social lender and so was aware of alternatives to the major banks. Further research established that we were a viable potential lender and the trustees approached us for a loan.

Applying for a loan had not been part of the charity’s project plans and they were unprepared for the extent of the application process, which requires the completion of extensive paperwork.

There was definitely a steep learning curve for both the charity staff and trustees, who acknowledge that in hindsight, they had underestimated the rigorous due diligence process. Through regular face-to-face meetings, we were able to support them through the application process and assist with unfamiliar documentation.

Making it work

Since the redevelopment, the charity’s annual visitor numbers have more than tripled. Its site is open on more days of the week, necessitating the hire of additional staff, although the increased income has outweighed the increased expenditure. Located in a rural area, the charity’s newly raised profile and increased visitor numbers
has helped to benefit the local economy, increasing traffic to the local village shops, pubs and cafés. The charity itself has been nominated for and won several awards in its field and its future appears secure.

A fundamental key to the success of this loan was the strength of the charity’s original business plan, which had carefully and accurately weighed up the costs of the redevelopment against the projected improvements to its financial performance. Securing the loan from us gave the trustees the confidence to move forward and stick to their original project timescale, rather than waiting to obtain more grant money.

The key learning for us is to be clear at the outset about the extent of the loan application process. There is often a knowledge gap for organisations seeking social investment for the first time. We have a responsibility to bridge this gap and lend support where needed. Meeting potential borrowers face-to-face is an important first step in this process.

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