Bridging Loan - What does it mean?

Many grants are paid in arrears (and some are also paid late) and some contracts will also be paid at the end of the term. This can lead to short-term cashflow shortfalls. This type of loan enables an organisation to manage these mismatches in the timings of income and expenditure (i.e. temporary shortfalls). The loan is repaid when the delayed payment is finally received.

Who might use it?

It can underpin a short-term cashflow shortfall before a committed grant or other secured income is actually received by an organisation. It is a low risk facility as there is a guaranteed repayment of the lender's funds once the income in arrears is paid. Therefore, the interest rate on this type of facility will typically be low.

As long as an organisation can show that there will be a grant or other income being paid at a specific point, a loan facility can help solve tricky timing issues where there is a mismatch between the timing of income and expenditure.

Growth / Developmental capital - What does it mean?

This is capital that will be invested in a start-up or for the significant growth of a civil society organisation for the development of its products, services or projects which may generate surplus income.

Who might use it?

Organisations that have plans to grow will be able to use this capital as the majority of charities and social enterprises use their income and expenditure directly on day-to-day activities, leaving little surplus in reserves. This leads to an inability to invest in innovation and development, which are important for the long-term robustness and growth of the organisation.

Growth and development may be achieved through investment in "assets" as these have the potential to generate additional income. It may also take the form of an upfront investment to seize a market opportunity. Financial instruments such as equity, quasi-equity and patient capital can support and supplement grant funding for such capacity building. 'Hard' development capital refers to investment in property or other tangible assets. 'Soft' development capital describes investment in products or services, e.g. additional staff for fundraising support.

Secured Loan - What does it mean?

The borrower will pledge a tangible asset (known as "collateral") such as a building or equipment to receive a loan. In the event of a default, the lender can take possession of the asset which can then be sold to recoup the loan. A long-term, secured loan on property is known as a "mortgage".

Who might use it?

An organisation that owns an asset will be able to secure a loan against this asset for a variety of purposes such as growth, working capital or for specific projects. This security reduces the risk for the lender; thereby reducing the loan interest rate. The lender will have a fall-back option of selling the asset in the event of a default. The security is typically in the form of property or equipment, but can also be cash deposits.

The borrower must still demonstrate that it will be able to repay the loan from its income streams as the lender would rather have this than take the more expensive route of selling the collateral. If a loan has a term of more than 5 years, it will usually need to be secured as there is less certainty about future income to repay the loan.

Working Capital facility - What does it mean?

Many organisations can have cashflow problems due to the timing differences between outgoing and incoming payments and the lack of cash reserves. This facility is used to finance the everyday operations of an organisation.

Who might use it?

An organisation may have a shortage owing to the time lapse between bills being paid and invoices being settled. This type of loan will fill these 'gaps', enabling an organisation to function normally until operating expenses can be consistently covered by revenue. This facility can be in the form of an unsecured loan, overdraft, standby facility, an equity or quasi-equity investment.

An organisation can have assets or run profitable activities, but be short of liquidity if its assets cannot readily be converted into cash. This facility is required to ensure that an organisation is able to continue its operations and that it has sufficient funds to meet its operational expenses.

The funds can be used for everyday use, for example to pay rent, utilities, salaries, inventory and marketing, to counter any 'lumpy' income streams.

Equity investment - What does it mean?

This means investment through the purchase of share capital. If a civil society organisation's legal structure allows it (i.e. a company limited by shares), it can sell its shares to individuals or institutions. The funds can then be used for start-up, growth or working capital.

Who might use it?

A company limited by shares is able to sell some or all of its shares to investors. However, this may dilute ownership and control of the company as shareholders may be able to make their demands on the management team to change operational strategy. Investors will also expect dividends, so not all funds will be re-invested in to the company.

Most civil society organisations are constituted as companies limited by guarantee. (i.e. with no share capital) and so equity investments are generally rare. Additionally, exit strategies are not always forthcoming as equity offerings in the social sector are typically illiquid (there are few opportunities to buy and sell equity in civil society organisations). There is no established market for the shares, so it may take a long time before another investor can be found to exchange shares. Shares in the sector are typically traded on a "matched bargain" basis by a broker, rather than on a stock exchange.

Community Investment - What does it mean?

It works by selling a share in an enterprise to people in the community. These people, as shareholders, control the enterprise. Members of a Co-operative Society or Community Benefit Society can become shareholders and invest in local enterprises providing goods and services that meet local needs. Members only expect a fair and modest return on their investment. The return payable is based on the principle that interest should be no more than is sufficient to attract and retain the investment. Members invest on the understanding they will be rewarded primarily through a social dividend rather than a monetary dividend.

This long-term alignment of the interests of owners, investors and customers, is at the heart of the community enterprise movement. And this works best when the community purpose of the enterprise is the primary motive for investment. The central task of all community shares initiatives is to build membership. This works by selling a share in an enterprise to people in the community, who become members of the enterprise. These people, as members and shareholders, control the enterprise.

Who might use it?

People or communities who want to raise finance for a community project or resource that will generate its own income, like a building, a shop, renewable energy project or other community enterprise. This approach will only work if there is, at least potentially, a community that is willing and able to support the enterprise. It starts with community engagement.

Ownership and investment go together to form a strong bond, engaging communities in enterprises that serve their interests. Investors are more likely to become loyal customers, volunteers and activists that support the enterprise in achieving its community purpose. The approach can strengthen the business model, but it also carries the risk that people's money will be lost or their expectations will not be met. So part of community engagement must also be about community education, ensuring that people understand the enterprise, the risks they are taking, and what they can do to make the enterprise sustainable.