



Analysing the concept of 'Social Stock Exchange' in India

July 2020

home.kpmg/in

Table of contents

1. Context setting	1
2. What is a Social Stock Exchange?	3
3. Global models of SSE	5
• Canada – SVX	6
• Singapore – IIX	6
• South africa – SASIX	7
• United kingdom – SSX	7
4. Social Stock Exchange in india: a proposed model	9
• Strategic framework	9
• Operational framework	11
• Challenges and mitigation measures	14
5. Way forward for institutionalising an SSE in India	15
• Roles of key stakeholders	15
• Implementation plan	16
6. Conclusion	17
7. Appendix 1: Process to enlist social enterprise on SSE	19
8. Appendix 2: About ngo-darpan portal	20

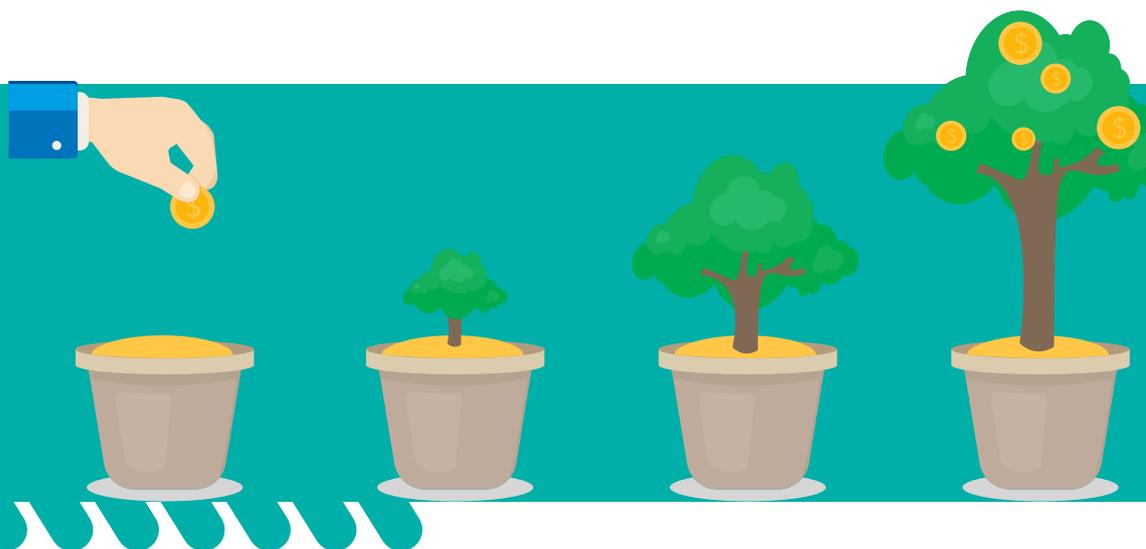


List of figures

1. Figure 1: Expenditure numbers as per UNDP Human Development Report 2019	1
2. Figure 2: Representative model of SSE	3
3. Figure 3: Proposed model for SSE in India	10
4. Figure 4: Suggestive workflow to enlist entity on SSE	19

1

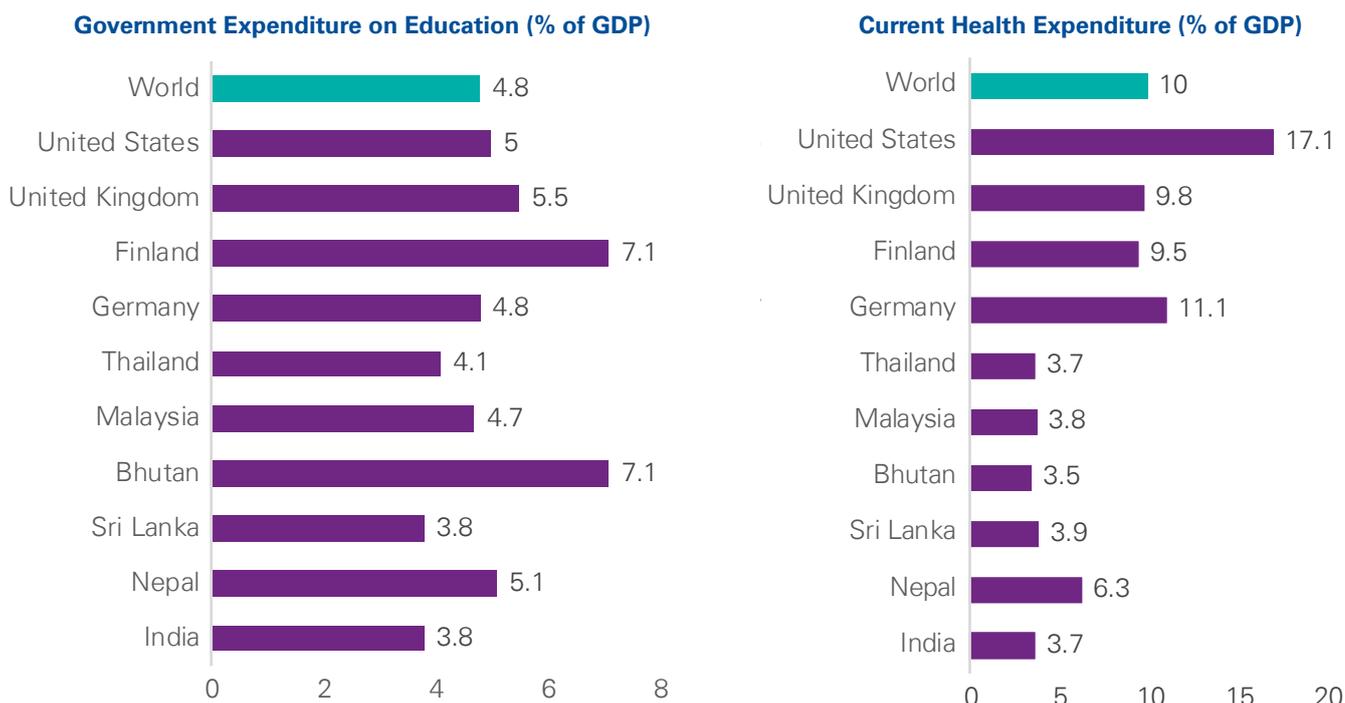
Context setting



The social sector has been a driving force in India's developing economy with a host of organisations working to empower local communities and develop resilience to the drudgery of poverty, climate change and other socio-economic problems. Mainly focused on reducing the perils facing the disadvantaged sections of society pertaining to healthcare, education, gender, livelihood, sanitation

and various humanitarian causes, social organisations have been quintessential partners in ameliorating some of these developmental challenges that the country is facing. As per the Human Development Report, 2019 by UNDP,¹ India records the lowest public education expenditure and health expenditure figures as a percentage of Gross Domestic Product (GDP) in the world as shown in the charts given below.

Figure 1: Expenditure numbers as per UNDP Human Development Report 2019



Taking cognisance of the sheer magnitude of these problems, governments across the world have started forging partnerships with the private sector and philanthropy outfits to operationalise the strategies to overcome such pressing problems. There are a number of entities working in the social sector - while a non-governmental organisation (NGO) is a non-profit social service voluntary organisation (VO) of communities, persons, volunteers, civilians and citizens, a social enterprise or a for-profit organisation is a revenue-generating business with the primary objective of achieving social good. Social enterprises, unlike NGOs, operate just like traditional businesses with the exception that the profit generated is usually not used as a pay-out to investors but reinvested into the social programmes. In FY 2018, the total social sector financing in India stood at INR 2.8² lakh crore, having grown at a rate of 11² per cent every year from 2014 to 2018. The funding support to the social sector mainly comes from four sources: government spending, individual contributions, donations from and High Net Individuals (HNIs), international aid and Corporate Social Responsibility (CSR). While CSR can facilitate close to INR 20,000-25,000³ crore to social development, only around 30³ per cent of leading firms are obligated to fulfil CSR and/or collaborate with NGOs since most of them have their own foundations. The foreign funding component has also faced a 40⁴ per cent decline in the four years ended 31 March 2018,

due to crackdown by the government following violation of the Foreign Contribution Regulation Act, 2010. Hence, funding for social causes has been a domain fraught with challenges for some time now. In the latter years of the 20th century, India was introduced to the phenomenon of impact investing, an approach that merges financial investment with achieving goals in the developmental sector. According to Global Impact Investing Network⁵ (GIIN), impact investments are investments made into companies, organisations and funds with the intention to generate social and environmental impact alongside a financial return. The key characteristics of impact investing are financial returns (return of capital to risk-adjusted market rate returns), intent to generate a positive social impact through investments and, in select cases, commitment of investors to measure the social performance of underlying investments.

Impact investing in India has witnessed growth over the last few years. It is estimated that over USD 5 billion has been invested between 2010 and 2016, with more than USD 1⁶ billion invested in 2016 alone. Majority of this funding is invested in the form of mezzanine debt. Other instruments include grants, equity, guarantee and quasi-equity modes. To invigorate impact investing in India, another innovative model, the social or development impact bond that employs outcome-based or pay-for-success financing, has also made its presence in the country. It is, however, only at a nascent stage,

with two contracted in education and one in healthcare. Impact bonds offer an outcome-based, mission-aligned investment opportunity to investors, provide upfront funding the service providers thereby minimising financial and operational risk of the outcome funder (such as the government in case of social impact bonds and philanthropic organisations in case of development impact bonds). Despite the advent of numerous financing options, organisations in the social sector continue to face fund scarcity coupled with challenges of access that make the funding process a tough row to hoe. Some of the issues faced by the stakeholders include the volatile nature of the sector, shortage of discerning investors who work with impact enterprises, especially those based in rural India, lack of transparency and exit opportunities, standardised frameworks for impact evaluation, limitations for local funds as investors set up overseas funds due to tax implications and non-alignment of objectives of the investee organisation with that of the investors, among others.

Addressing the lack of funding opportunities available for social organisations, the Finance Minister, Ms. Nirmala Sitharaman announced the creation of an SSE, an electronic, transparent fund-raising platform for the social sector with the Securities and Board Exchange of India (SEBI) as a regulator. In her maiden Budget speech in July 2019, she called upon the capital markets to be closer to the masses wherein the idea was mooted to have a single-window solution in this funding conundrum.

2.

What is a Social Stock Exchange?



A Social Stock Exchange (SSE) is a platform to bring together social organisations and impact investors, especially institutional investors whereby the latter can buy stake in the form of bonds from listed organisations whose mission is aligned to that of the investors' interests. It operates like a regular stock exchange by facilitating listing, trading and settlement of shares, bonds and other financial instruments except that instead of solely a profit and loss status, the listed companies are required to

demonstrate social and environmental impact reporting in addition to their traditional financial reporting. SSE provides a mechanism to raise capital while preserving the social and environmental mission of the organisations, giving the investors diverse and viable opportunities to mitigate socio-economic problems through investments that also have the potential to produce financial returns. An illustrative model capturing the key components of an SSE is presented below.

Figure 2: Representative model of SSE



Some of the key benefits of a Social Stock Exchange include the following.

Improved market access – an SSE would facilitate a common and a structured meeting ground between social enterprises and VOs and impact investors with inbuilt regulation for providing sanctity and accountability of finances and ensure larger visibility of investors and investees. Moreover, potential investors would be saving costs on acquisition of credible information and background verification of potential investees. By defining project-level parameters for establishing overarching guiding principles for calculations, an SSE would ensure ease of capital inflow and outflow in a planned manner, minimising discordance between investees and investors together with preventing any disruption of benefits to the end beneficiary.

Transparency and accountability of social investing – given the rigorous due-diligence and performance metrics that an SSE would be installing for impact issuers and the background checks for investors, the platform would allow setting up of a credible information base. Moreover, these processes would also assist in installing a transparent and accountable system for transactions to take place. The performance evaluation of the social enterprises and the nature of the projects would allow them to attract higher ratings on the enlisted KPIs together with the necessary safeguards against malpractices for securing the investors' interests.

Synergy between investor and investee in social aims – in view of flexibility of investments and capital that would be available on an SSE, the canvas of choice would be much wider allowing investors and investees with similar missions and visions to connect seamlessly. This, in turn, would ensure joint ownership of the cause at hand and promote active participation on realising social objectives in a holistic manner.

Continued stream of finance – by allowing social enterprises a larger visibility to potential investors, the said projects and/or social enterprises would always have multiple options of capital inflow, resolving constant fears of fund crisis and abrupt closure of projects.

Performance-based philanthropy – given that performance of the enterprises listed on an SSE would be closely monitored and better ratings would increase their investment attractiveness, benefits and strategies implemented for generating impact for those at the bottom of the pyramid would be strengthened further.

Market discipline and healthy competition – owing to inclusion of impact ratings and a grading mechanism, an SSE will induce market discipline and foster healthy competition among the impact issuers to be able to achieve social goals. Additionally, an SSE is likely to transition the impact investment space into a much more regulated space with focus on sustainable development.

Reduced burden on government – the Central and State governments till date have the biggest onus of achieving sustainable development goals. The setting up of an SSE would greatly leverage private sector participation in some key areas allowing the government's burden to be reduced to a certain extent while engendering a collaborative approach in achieving the development goals

Access to international finance – an SSE would form a platform for leveraging and attracting foreign funds and funds from bilateral and multilateral agencies in a streamlined manner. The platform would give access to these agencies to play a key role in the development of the social sector of the country while also verifying their credibility in due course. In the long run, this would, in some ways, curtail the influx of dubious foreign funds in NGOs and VOs.

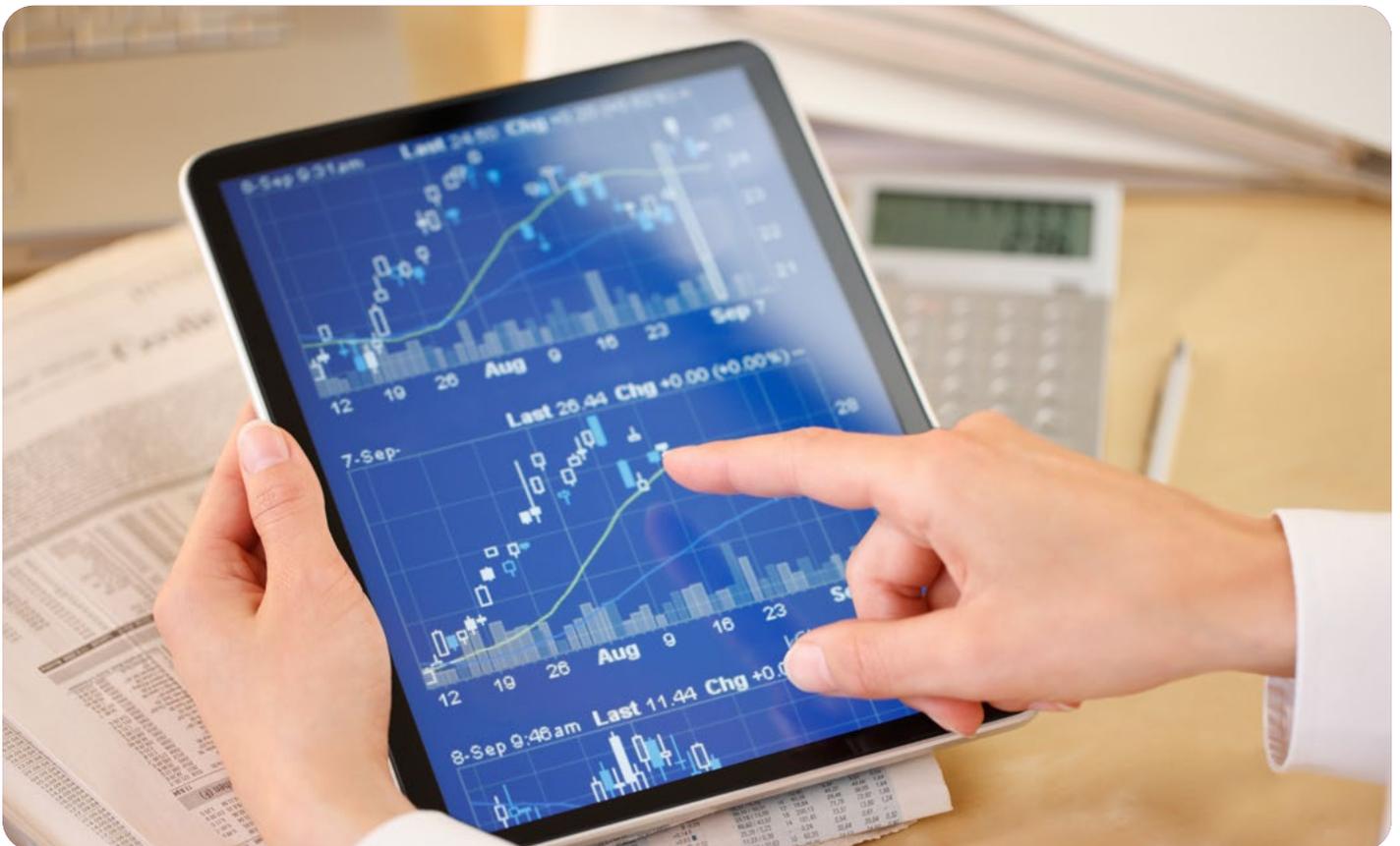
3.

Global models of Social Stock Exchange



Globally, SSE is a fast-maturing concept and functions differently suiting the needs of the native development sector. While India seeks to propel its growth story in the social sector space, there are a few models that can be emulated,

garnering their expertise and relevance to the Indian context. Within the purview of this paper, we have looked at the working models of four countries.'





Canada – SVX⁷

Canada's Social Venture Connexion (SVX), opened in 2013 and is backed by the Government of Ontario. It is an online platform that uses crowdfunding and private placement to support capital raising by impact ventures and funds. For social businesses and organisations, SVX allows provisions to list organisations and its securities, tailor fundraising requirements and attract investors. For potential investors, it offers access to investment opportunities in the social sector. Investors and issuers can manage their investments on the platform, have 24-hour access to all documents in one place and make transactions through the platform. The sectors catered to by SVX include cleantech, health, work and learning, food and social inclusion.

The broad range of securities made through SVX includes common shares, preferred shares, bonds, convertible debentures and fund units and currently no secondary trading allowed. The platform currently hosts Ontario-based impact ventures and funds, including not-for-profits and charities and for-profit businesses. SVX also reviews issuers to ensure that they meet SVX's impact criteria and charges a fee for application, profile review and future transactions. It uses Impact Reporting and Investment Standards (IRIS) metrics to evaluate impact or certificate issued by a B Corporation (leading firm in Canada issuing certificates to firms that meet highest standards of social and environment standards) thereby providing uniformity to investors in valuing the business.

On the investor front, only accredited investors are permitted to access SVX, which include foundations and endowments, asset managers, wealth advisors and HNIs. To regulate the conduct of investors and ensure durability of the investment, the exchange uses an SVX investor agreement which states that the investor acknowledges the fact that his/her investment might not bear any financial returns hence weeds out those investors who prioritise profit over any social gain. At present, SVX has 12⁸ social enterprise issuers and has helped mobilise USD 100 mn (~INR 750 crore) in impact capital for over 100⁹ ventures in their programme.

Singapore – IIX¹⁰

Opened in 2013, the Impact Investment Exchange (IIX) in Singapore is based on a crowd-funding model that allows mature social enterprises to raise capital by issuing securities to a larger group of investors on a public platform that facilitates trading in listed securities (including shares and bonds). Running in partnership with Stock Exchange of Mauritius (SEM), IIX provides exposure to global base of limited and accredited impact investors looking for transparent and liquid investment opportunities. Sectors focused by IIX include energy, agriculture, education, healthcare and water.

While regulated by the financial services commission and operated by SEM, IIX screens potential issues on the impact eligibility criteria and provides recommendations to SEM. In addition to the Social Return on Investment (SRoI) framework which measures how much social and environmental impact (in dollar figures) is created for every dollar invested into programme, IIX also uses the IRIS metric. Additionally, the exchange mandates the potential impact issuers to appoint an authorised impact representative (AIR) to ensure that social enterprises stay true to their commitments in terms of appropriate usage of capital, compliance to corporate governance norms and financial integrity, thereby safeguarding the interest of investors.

IIX's USD 20¹⁰ million (~INR150 crore) women's livelihood bond was the first instrument listed on the impact exchange.¹¹ It was the first in the series of IIX sustainability bonds (ISB). ISBs are financial instruments used to mobilise large scale private capital by pooling together a group of impact enterprises and are replicable in nature, meaning, they can be customised to suit different geographies, sectors etc. While being similar to the UK's SSX model in some ways, the Singapore model also includes non-profits in the sector who can issue debt instruments like bonds. Having built a network of over 30,000 partners, IIX Singapore is successfully helping raise an impact investment capital of around USD 40¹⁰ million (~INR 300 crore) per year.



South Africa – SASIX¹²

GreaterGood South Africa Trust's initiative and supported by Noah Financial Innovation's Broking for Good Foundation, South African Social Investment Exchange (SASIX) was set up in 2006. Tied with the Johannesburg Stock Exchange, SASIX works like a conventional stock exchange allowing ethical investors to start investing from as little as Rand 50¹³ (~INR 200) to, in turn, get a tax benefit. Investors can browse their website and select social businesses based on project type, sector and province. They can also keep track of the way the projects are being delivered and impact generated.

SASIX applies the same sort of assessment and due diligence considerations to projects as would be applied to financial investments. The platform seeks to increase the participation from the public, corporations and civil society in the social development of South Africa. The exchange ensures a level playing field by providing access to capital for small, pioneering and remote organisations and investors who want to invest in one project or a portfolio of projects – by purchasing shares online or through the offices of the GreaterGood South Africa Trust. In addition to this, GreaterGood South Africa provides analysis of the achieved outcomes and an assessment of the lessons learned at the end of the social investment cycle.

Moreover, in case where the project is listed for more than twelve months without receiving enough funding, the project offering gets expired and the option of allocating the contribution to another SASIX project becomes available to the investor. In case the investor chooses to close his account in SASIX, the money in his account is allocated to the sector/entity of his choice but is not returned as the investor has already received the tax benefits for the same. Fidentia Group is enabling the operations of SASIX by providing essential administrative, financial and trust fund management support services.

Started with an initial offering of 15 projects, SASIX has made a significant contribution to South African development with over R34.6¹⁴ million (~INR 13.84 crore) invested in 53 social development projects in over two years of its start. With a focus on early childhood education, orphans and vulnerable children, food security, enterprise development, the enlisted projects have shown measurable social impact.



United Kingdom – SSX¹⁵

The social stock exchange in London serves as a directory, listing down social organisations for investors to invest in. It does not facilitate trading of equity but acts as a research platform and helps connect potential impact investors with social organisations. It acts as an information provider publishing standardised and comparable social impact data on listed organisations. For any organisation to be listed on the social stock exchange, it must be registered in the London Stock Exchange and has to successfully undergo a social impact test conducted by independent experts.

The social impact test is a stringent check on understanding whether the organisation has the potential to deliver viable returns and demonstrate how they will adhere to their own social and/or environmental mandates and missions. The social impact test measures the impact of organisations in terms of the social or environmental mission of the social business; target beneficiaries; details on a business's products, services and operations that deliver that social impact; stakeholder engagement and consultation plan; evidence of social impact, means of collation, measurement and reporting of such impact.

Over time the U.K.'s Social Stock Exchange has become a strong information repository with a base of 36 member companies and its members have raised GBP 400¹⁵ million (~INR 37,200 crore) for, among other things, affordable housing, clean energy and new healthcare facilities.

The UK SSE does not facilitate transactions whereas in countries such as Canada or Singapore, SSE works as a crowdfunding¹⁶ platform for impact investors to invest in social enterprises that match their investment objectives. The aforementioned SSEs cater to their country's requirements and offer a great insight in understanding the strengths and weaknesses of the system.



4.

Social Stock Exchange in India: A proposed model



With the rise in impact investing in India, institutional investors are gradually realising the potential of investing in the social sector, apart from tertiary meeting CSR objectives. However, these investments are not enough to bridge the overall development gap. An SSE in the Indian context should function as an effective tool to

address the financial concerns of the sector while promoting sustainable development. In addition to working as a repository of social enterprises, an SSE should facilitate real-time transactions in the social sector. In subsequent sections, a suggestive working model for SSE in India has been discussed in detail.

Strategic framework

While designing a strategic outlay of an Indian SSE, a KPMG in India's value chain model (STRIVE) has been used. It includes the following.

Stakeholder value chain – covering a host of VOs and social enterprises from the development sector, the SSE will link them with institutional (and retail) investors to achieve the said goals. In addition to this, an SSE is envisaged to create linkages with support units such as certifying bodies (to rate impact), technology partners (to help transaction processing), legal and regulatory authorities, impact evaluators, among others. An SSE is expected to create a transparent and accountable social ecosystem in the country, resulting in last-mile impact.

Technology and platform – for managing a full-fledged SSE ecosystem with high volumes of transaction, there is a need for strong technology integration and creation of robust underlying platform. It is also important to have basic facilities and select SSE operations to operate both in online and offline modes, factoring in the needs of rural and semi-rural entities, which would be associating with the exchange platform.

Returns and impact – higher weightage will be given to social impact instead of financial performance. Additionally, it is important to ascertain the actual impact generated on the ground against every rupee of investment. An SSE will enable a structure of monitoring and reporting of impact against a predefined metric.

Institutional structure – an SSE will not only open avenues to raise capital but also will make the process standardised over time by creating a single window solution for connecting investees and investors. The SSE should therefore have a strong institutional framework with adequate participation from both the demand as well as the supply side along with representation from Govt. and other regulatory authorities. A strong structure will induce transparency and fairness to transactions. The key to a strong governing board will be to include stakeholders from across the impact value chain for enhancing participation

Value creation – it is envisioned that the SSE would function as a repository of social enterprises and VOs and proposed to fulfil the objectives as laid out in the national policy on the voluntary sector (notified in 2007). To meet the same, there will be mechanisms to introduce ranking for social enterprises and investors

basis the completed projects in order to ensure that the focus is on the social sector. The theory of change methodology would be followed for planning and execution of projects to promote social endeavour. It will map long-term goals and strategic objectives of impact organisations and a reverse-mapping matrix to

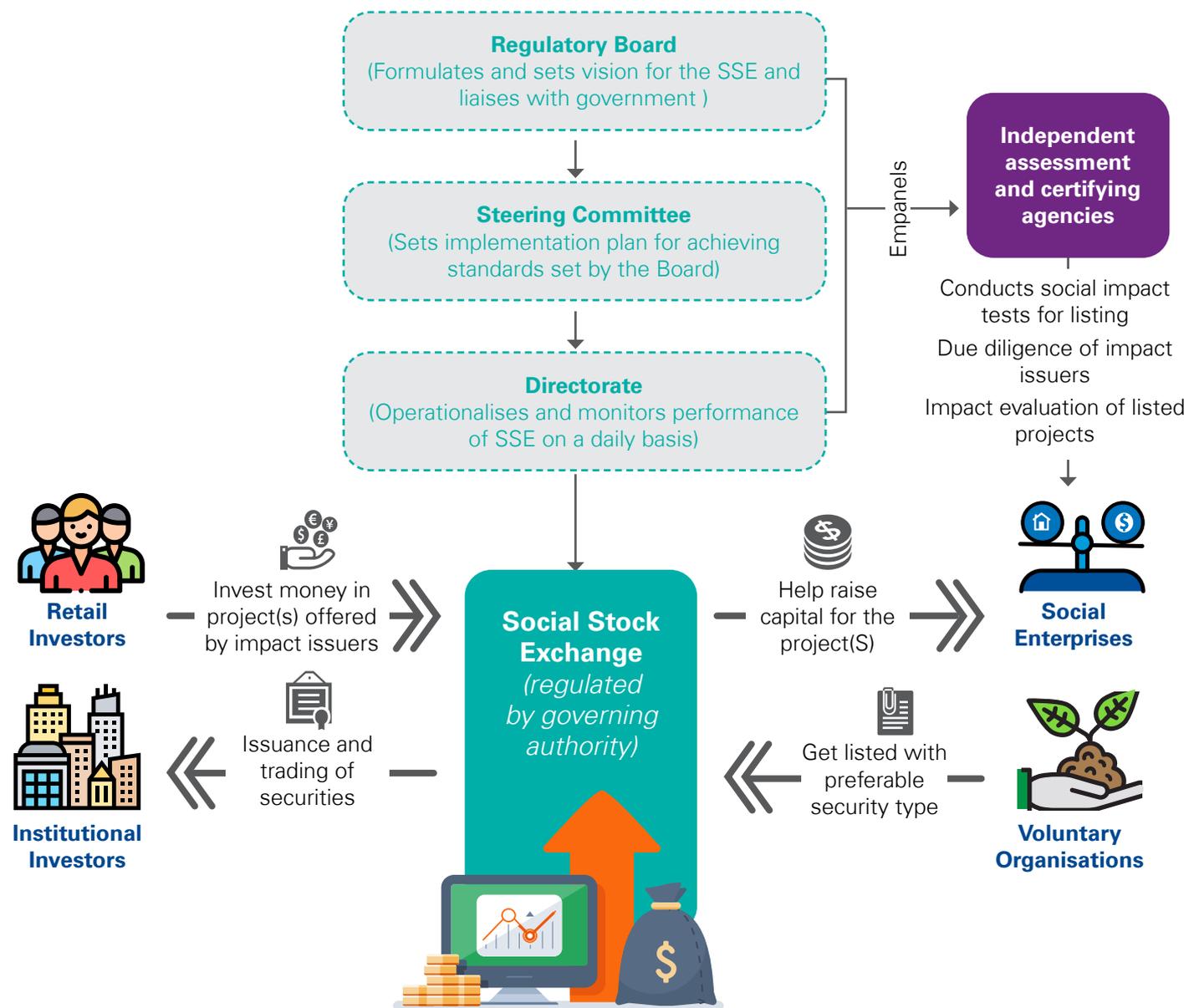
understand prerequisites to achieve such objectives.

Educate and capacity building – a critical element to creating awareness amongst the stakeholders would be to educate the ecosystem on the characteristics of an SSE, impact investing, financial inclusion, while building capacity of investees

as well as investors and expanding the outreach efforts in India's social sector. Focused planning to on-board the right stakeholders would be imperative for successful operations of an SSE.

An illustrative model of an Indian SSE has been provided below:

Figure 3: Proposed model for SSE in India



Operational framework



An SSE in India will function as a trading platform, providing capital to social enterprises and VOs in a transparent and efficient manner, while ensuring social impact and safeguarding the interest of the investors. As part of its operational mechanics, the key considerations have been listed in the below sections.



The change agents – sustainable and viable enterprises would be encouraged to benefit from the SSE including NGOs which seek funding to create last-mile impact without any financial gain. An initial task would be to clearly map the types of organisations that can be listed on the platform. Different channels of fund allocation, due diligence frameworks and social impact metrics would be essential to build a steady flow of users on an SSE. From an investee standpoint, the type(s) of potential entities that can be listed on an SSE could include section 8 companies; companies limited by guarantee; private and public limited companies having social welfare as their objective; trusts; NGOs; social sector associations; co-operative societies; social mutual funds; social AIFs (alternate investments funds) etc.

Social enterprises and VOs would need to undergo an impact filter conducted by independent agencies before getting listed on the SSE. This is to ensure a transparent process is followed for baselining the impact and in turn boost investors' confidence. The independent agencies would evaluate and assign an impact score to the enterprises by following a standardised impact test against predefined metrics to deem enterprises eligible or ineligible to be listed on the SSE (basis the scores achieved). Additionally, these rating agencies would be formulating a rating cum grading mechanism basis social and key financial parameters for continual evaluation

From the investment standpoint, impact investors including retail investors; social venture capital funds; corporate or institutional investors; in select cases, govt., and quasi-govt. bodies, will be providing the capital to social enterprises/VOs using different financial instruments. To mobilise the investors, it is important to safeguard their interests and provide them channels for primary and secondary market transactions. In the initial

phases of launch of an SSE, Govt. and an SSE governing board should work closely with regulatory authorities as well as the impact investors to design regulatory and impact parameters.



Governance structure – for operationalising the SSE, a strong and a robust governance framework needs to be institutionalised. This hierarchy of agencies and personnel would be steering, driving and executing the social stock exchange's mission and implementation objectives. A proposed governance structure for the SSE would consist of the following levels.

- **Governing board:** situated at the apex level, this board would be responsible for providing the overall guidance and liaising with the government in order to help devise policies to compliment the working of the SSE. With key representatives from the government and the industry, the board would be setting the priority areas and initiatives for the SSE while also reviewing its progress and development
- **Steering or working committee:** chaired by a senior government official or thought leaders in the social sector space, a steering committee would be responsible for planning and setting the milestones for achieving the mission statement as set by the governing board. Together with monitoring and evaluating the performance of the SSE, the committee would also be responsible for detailing out norms related to entry, continuance of listed entities while setting the financial thresholds of trading and related regulation
- **Directorate:** it would consist of the executive wing with a responsibility to operationalise the exchange on a day to day basis. With a management structure in place, it would be coordinating the efforts of investors, investees, certifying agencies and regulators in the working of the SSE. While converging the efforts of the stakeholders and providing end-to-end solutions of implementation of the exchange, the directorate would be closely monitoring the overall working of the SSE.

It is imperative that in the governing board and the steering committee, representatives from the side of the investors, investees, government and certifying agencies find a place to draw on a democratic and comprehensive representative base for decision making. This would

also allow the SSE to work holistically incorporating the nuances and viewpoints of all related stakeholders.



Due diligence and concurrent monitoring – one of the most critical elements of the operational framework is to enable strong quality assurance and regulate the listing and impact evaluation process. There are two key phases in this step viz. due diligence at the time of listing of entities and concurrent monitoring. In order to prioritise sustainable and high impact models in the developmental sector, it is essential to develop robust eligibility criteria along with social and financial disclosures. This would help in shortlisting the credible entities to be listed on the SSE. This would be followed by assignment of an impact score by an independent rating agency. A brief overview of the listing process is provided in appendix 1. With an objective to support social enterprises in creating on-ground impact, higher weightage would be assigned to social considerations over financial.

Once the entity is listed on the platform, the process of concurrent monitoring would begin. The investee would need to update the project's progress and share fund utilisation certificates at predefined intervals. This would help in better planning and forecasting of subsequent fund requirements and achieving the envisaged impact.



Financial instruments and trading of securities – the SSE would operate as a full-fledged marketplace wherein trading of securities issued by social enterprises via multiple instruments would take place. There would be primarily three gates for fund mobilisation viz. debt, equity and grant or CSR gates, depending upon the nature of the impact issuer and its capital needs. While the equity gate is appropriate wherein the impact issuer is ready to share part ownership with impact investors and investors are highly motivated for comparatively risky investment, the debt gate would be considered when the impact issuer wants to raise funds through secured loans or debentures. The third gate is for aid which facilitates one sided donation from impact investors to impact issuers, without any expectation of financial returns. In order to facilitate trading through debt and equity instruments, there will be provision of limiting the amount that may be raised through grants.

As the SSE will be a new age platform, other classes of financial instruments must be also be explored, such as social mutual funds, social REITs (Real Estate Investment Trusts) and social securitised products. However, it is recommended to enforce these products in a phased manner to ensure sustainable SSE growth, without disturbing the confidence of investors and the morale of the investees. For instance – social mutual fund is

a recent phenomenon. India has recently introduced socially responsible or ESG (Environment, Social and Governance) mutual funds which invest in companies that are committed towards the environment and society and score high on three¹⁷ parameters i.e. environment friendliness, social responsibility, and governance. Social securitised products have remained relatively underdeveloped because of the unique challenges they face such as involvement of multiple parties i.e. borrower (impact venture), lender (loan provider) and issuer (special purpose vehicle) – complicated structure and unique underlying asset.

The primary means of raising funds for social enterprises listed on an SSE would be through issuing securities in the form of various debt and equity instruments and investors would be allowed to invest in the entities of their choice by buying these securities with an inherent possibility of trading with future investors. The process would include the following.

- Impact investors do a thorough analysis of listed entities basis impact score, nature of the listed project, operational history and financial performance to take investment decisions
- Investors opt for securities of the selected entity leading to capital infusion. They may also trade their securities with other potential investors (possible avenue of acquiring securities)
- The impact score, milestones of the project, demand and availability of a listed entity's securities would determine the price of the securities for trading in the stock exchange.

Calculating returns on investments – the returns, both financial and social, of impact investment depends on a variety of factors. The financial returns to the investors are contingent upon the achievement of a pre-determined target outcome of the social enterprises. On the other front, there exists a number of tools and metrics in conjunction with SRoI to assess the value created by social enterprise. SRoI provides a process to determine how to measure value and forecast social returns. The reporting frameworks and investment standards ensure alignment of financial accounting rules alongside impact performance accounting. It enables estimation of the financial value of the social or environmental good likely to result from each rupee invested.

In case where the project has been able to generate impact that can be appraised in monetary terms, social enterprises can simply reinvest it in the project undertaken. However, in projects where the financial returns are expected, the option of converting financial return into social return points by ascertaining the value

equivalent to the amount gained and crediting the same into the account of investor can also be explored. Also, for all the successfully implemented projects, the social impact of the impact issuer would be positively aligned (improvement in the impact score) for inducing higher credibility during the investors' evaluation in future listing of the projects.

Apart from this two-dimensional model involving investors and investees, an SSE may also look upon the three-dimensional model being followed by development impact bonds i.e. involvement of private investors, impact issuers and outcome payers.¹⁸ While the investors provide upfront working capital to impact issuers to carry out development projects, the outcome payer is responsible for paying out to the investors if the pre-specified measurable social outcomes are achieved. In some cases, the outcome payer also funds the costs of measuring the impact created by the impact issuer on the ground. The impact issuer, usually an NGO, works to deliver the social outcomes and deploys solutions on the ground. Similarly, the entities listed on an SSE can consider replicating the model wherein government bodies can become the outcome payer. Hence, an SSE should provide space for both concessionary and non-concessionary investors with a layered structured of participation depending on the levels of risk that the investor can embrace.



Impact evaluation – another critical element in the operational value-chain of an SSE is a process to undertake a systematic causal attribution for any intervention(s) planned by social enterprises. The benefit of impact evaluation is two-fold viz. it provides information on what worked and what did not work in a social impact project. Impact evaluation also helps in improving the implementation of the project (on an ongoing basis or for future projects). Impact varies with the type of project undertaken, geography of operations and also the type of investor (philanthropists, community development institutions, commercially astute investors, retail, or institutional impact investors). An SSE will deploy processes and techniques to standardise the measurement of impact across projects. Lately, some curated metrics have come up - the Impact Reporting and Investment Standards (IRIS) and a rating system known as the Global Impact Investment Rating System (GIIRS), Sustainability Accounting Standards Board (SASB) and Global Reporting Initiatives (GRI) Standards etc. While such metrics can look at measuring of outputs, which is, in a way, the first step towards assessing the outcomes, they at times fall short in judging the value of the long term.



Managing investors' interest – a key consideration for most investors is the need for ensuring a sustained inflow of both financial and social returns that the listed enterprises deem to deliver through their projects. However, due to unforeseen reasons, the said project may not be able to deliver the said outcomes and therefore the recovery is low or nil. An SSE must ensure that the governing guidelines and standard operating procedures are put in place to manoeuvre the situation, entailing the least harm to all the stakeholders. From investors' standpoint, capital protection is highly critical and is important to discuss upfront various options such as grant protection, inflation protection, sub-optimal guaranteed returns or commercial returns.

There exist different types of investors - those who are non-concessionary (not willing to make any financial sacrifice to achieve their social goals) and concessionary investors who are willing to make some financial sacrifice to achieve broader social goals. In philanthropy parlance, those opting for the former are driven more towards initiatives that are called mission-related investments (MRIs) and the latter towards programme-related investments (PRIs).¹⁹ The concessionary involvements would largely be geared towards the initial stages of social enterprises wherein they are trying to develop and establish a viable business model and financing the initial stages of tech-based companies looking to serve those at the bottom of the pyramid. The non-concessionary investors, however, would be drawn towards the second and third stages of the said organisations' growth wherein they are looking to scale up, refine processes and develop talent. The non-concessionary involvements could also be directed towards enterprises, which would deliver market returns but in addition the investment must mandatorily deliver some earmarked social or environmental outcome beyond what would have otherwise occurred.

Other solutions to manage investors' interests include risk adjusted return transferability i.e. investors can draw the said returns from allied projects that the impact issuer may have in other geographies (depending upon the alignment of theory of change). In case there are no such projects, the investee can look at issuance of shares as a short-term measure. Given the nature of the social sector, the gestation period is critical, and the investors should be allowed to exit only after the predefined and agreed upon milestone achievement. Alternatively, the initial investments could be made tax free (with a ceiling) to pass on the benefits to the investors. An SSE's governing board should also look at creating a pool of evergreen funds (from govt. bodies, international donors, and other wilful investors) which can service the investors' interests in times of any crisis.

Challenges and mitigation measures



Given the societal and market idiosyncrasies and the presence of a historically divided society in India, operationalising an exchange directing capital to socially embedded causes has its set of challenges. They emanate mainly from the nature of the entities and transactions. Some of the identified challenges and related mitigation measures are captured below.

 **Definition of a social enterprise** – with varied range of enterprises and organisations working to deliver ‘social good’, it is imperative to clearly define the contours of a social enterprise. From ideating on their governance and organisational structure to identifying a list of services they can provide, how social-environmental benefits would have to be the primary aspect of their project, all of it would have to be clearly defined upfront.

 **High transaction costs** – an SSE would attract players of all scales, leading to higher transactional costs in view of the institutional effort that would be required in due diligence, monitoring and subsequently impact evaluation. Means to outsource the ancillary functions or passing the costs on to the investors for the specified transactions needs to be planned. Such measures could also hamper participation of small-scale retail investors on the exchange; however, combined with tax benefits, this challenge can be addressed.

 **Investment readiness and the scope of emerging entities** – an SSE needs to focus on capacity building of social enterprises and listed organisations. This includes making them investment ready to be align with the needs of transparent financial systems, equipping them

with financing nuances etc. Moreover, since an SSE would mandate a rigorous financial and administrative scrutiny, it is essential that the parameters are well defined to ensure a broad spectrum of participation, including small scale entities.

 **Metric of impact evaluation and return on investments** – it is important to define a standard metric to measure the impact of social projects and thereby associate social and financial returns to them. However, owing to the nature of the sector, the impact varies from sector to geography to beneficiary. It will require an independent impact evaluator that is an expert in the impact investing space and can continuously curate and standardise the measurement metric.

 **Trading instruments and tax benefits** – an SSE would have to clearly delineate the financial instruments that would be traded for impact issuers and investors. In addition to this, trading of securities and tax related regulations must be clearly put in place. It is required that the tax laws in India relating to the social sector are synchronised and integrated to attract both investors and investees with the required incentives.



5.

Way forward for institutionalising an SSE in India



To institutionalise a viable SSE structure in India, it is imperative to build a comprehensive ecosystem which enables both investors as well as investees holistically. This includes services such as legal advice, project selection and tax regulations. A dedicated support channel must be established to help social enterprises and organisations through the listing process, run

continuous capacity building programmes and help them comply with the impact investment requirements among other areas. A well-defined SSE ecosystem would consist of lucid policies, investees familiar with impact investing, process of securities trading and potential investors who are well-informed and are willing to channelise their funds via an SSE.

Roles of key stakeholders

To steer growth and functioning of an SSE in India, the roles of various stakeholders become essential. In building the capacity at the sector level to leverage the benefits of an SSE, the Government of India and its affiliated regulatory body would be of great value. As policy makers, they would enable transactions by providing tax related guidelines for both national and foreign investors. Their role would be to establish the regulatory and legal framework laying down the norms of listing for both investors and investees together with curating a common framework of social impact assessment and benchmarking it to global standards to better integrate with international participants. In efforts to propel growth of the SSE, government must establish an incentive structure for investors and also develop a network of service providers, advisors who can assist on large investments, building provisions for social financing and preparing sustainable business and financial models. It is equally important to establish a strong due diligence mechanism for potential investors and investees wanting to get listed. Certifying or rating bodies would play a pivotal role in reviewing the social projects and adjudge

impact ratings. They could support the regulatory body in developing the eligibility criteria and the impact evaluation matrix. Periodically, these certifying bodies should also contribute to developing a repository of market intelligence and information on best practices in the impact investment space and assist regulators in building the capacities of potential investors and investees.

While the regulator and the certifying body form a part of the governance structure, investors and investees would be important from an impact funding and impact issuance standpoint, respectively. Investees would constantly follow market trends and best practices on impact investments and leverage the SSE to raise capital through issuance of tradeable securities. In ensuring a seamless listing process, investees would contribute towards complete disclosure during the due diligence process and strive to attain maximum impact ratings during and post listing of their social projects. The investees must continuously update their profiles on the SSE with the latest information on operations, financial performance, list of ongoing projects etc. Investors, however, would regularly scan through the listed projects or entities for investment purposes and share market

sentiments and social topics of importance. Working in consortium, the listed investors could fund capital and trade securities in projects aligned with their vision and mission of overall socio-economic development. They are expected to collect pay-outs against the investments as per the agreed terms in a timely manner, work with advisory groups, social sector practitioners and regulatory authorities to suggest improvements on rating and enlisting parameters and ways of attracting more investors on the platform.

Implementation plan

The announcement of an SSE in India was lauded as a progressive measure to focus on development sector initiatives. While many solutions and/or platforms can be used to operationalise an SSE, it is important that it

is accessible, equitable and of the highest quality. NITI Aayog, the policy think-tank of Govt. of India, maintains a portal – NGO Darpan. It is a repository of NGOs, VOs and acts as a platform for them to request grants from various Ministries or departments of the government. Entities obtain a unique ID by enrolling themselves on the portal. A detailed profile and current operational structure of the portal has been provided in appendix 2. The NGO-Darpan portal acts almost as a precursor (base platform) to the proposed SSE model. Profiles of the listed enterprises are vetted and they are equipped to raise grant from various govt. departments. However, the current structure of the platform only lets it function like a social directory. The existing features (and outreach efforts) can be leveraged and further built upon to scale it up as a full-fledged social stock exchange for the Indian developmental sector. This would result in time and resource optimisation.



Conclusion

As a concept, an SSE would shoulder enormous responsibility of streamlining capital inflow without compromising on benefits reaching those at the bottom of the pyramid. In its formative years, an SSE would need support and interest from institutional investors. Moreover, the government could also create financial capacities by leveraging funding support from public financial institutions, social mutual funds to enable priority investments into this exchange. For enlisting entities on an SSE, the scope of participation should be broad in keeping with the ethos of openness of exchange. In reference to marking net worth threshold of entry, an SSE and its regulator must take cognisance of the financial landscape of social enterprises in the country and ensure that only the credible and sustainable entities reap the benefits.

In view of the unified platform that an SSE would entail, foreign, multilateral, or bilateral entities may also be able to channelise their aid in a better manner. While addressing the quality assurance of listed social enterprises, an SSE can also create an e-KYI (know your investor) channel, ensuring a hygiene check - a more rigorous check point can be instituted for curbing the inflow of unscrupulous means of income. Much like the investee portfolio, even investors with a few thousands should be able to open an account and trade/invest in social projects. While allowing investors to create sector specific and/or region-specific funds, an SSE could provision the allotment of funds to different enterprises and projects in the related areas. In keeping with the diverse range of investors, an SSE should make direct market access possible for short-term, profit-making entities and long-term social return seeking ones while maintaining the social returns as its nucleus. Investors may be allowed tax benefits for donations given to such organisations (with certain minimum net worth). The tax exemptions could be rolled out in a phased manner wherein the

first investments of an investor can be made tax free and the secondary market transactions and profits emerging out of it may be tax exempted, initially for a stipulated number of years, to attract more investors.

In the last decade, over USD10²⁰ billion cumulative impact investments have been mobilised in the social sector in India leading to a positive impact on over 450¹⁵ million rural and semi-urban lives, generating employment and serving them through access to education, housing and better healthcare opportunities. The emergence of an SSE as a well-regulated platform holds a large opportunity to catalyse the impact of social investment thereby unlocking the unrealised potential of the industry and contributing to economic growth of the country. It is estimated that, in the next two years, if an SSE is able to facilitate around INR 500²¹ crore. of impact investments, more than 7¹⁶ lakh lives could be directly impacted in the areas of affordable housing, clean energy, food and agriculture, financial inclusion (~24¹⁶ per cent) and access to better healthcare (~40¹⁶ per cent). The impact investing space in India holds great promise to bring in additional finance to close the gap to be able to meet the United Nation's ambitious Sustainable Development Goals (SDG) targets by 2030. With India striving to clock the USD 5 trillion GDP mark by 2025, it is imperative that social growth is widespread and inclusive at the same time.

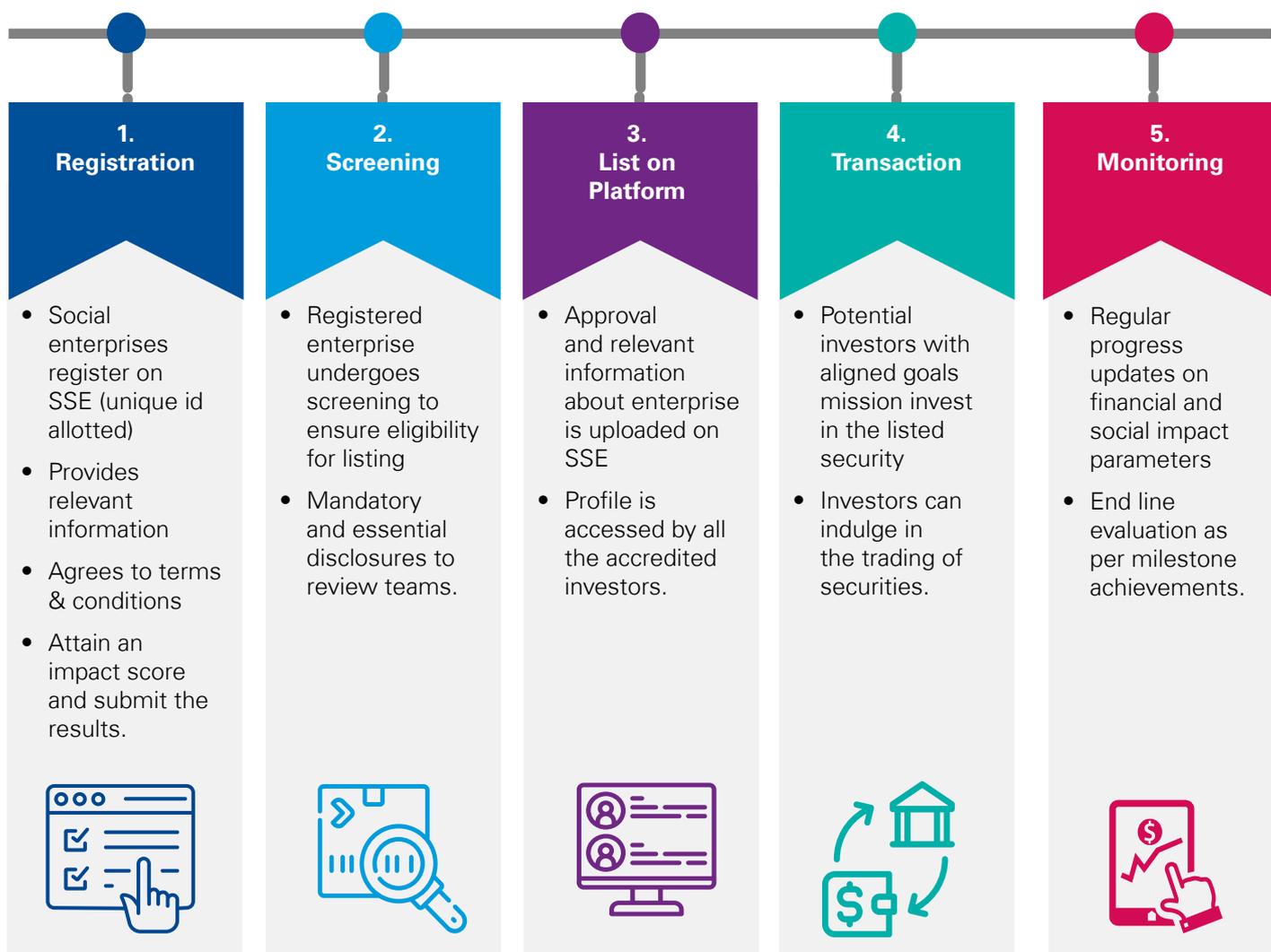


Appendix 1:

Process to enlist social enterprise on SSE

Figure 4: Suggestive workflow to enlist entity on SSE

Suggestive workflow has been captured below:



For scoring purposes, an independent certifying agency would list out parameters, basis which the impact score for the registered entity would be evaluated. This score would help potential investors understand the overall performance of the listed entities while making an investment decision. The process would be carried out at the time of listing and, thereafter, on a regular basis to keep an updated scorecard based on changing performance. Additionally, to safeguard the interest

of investors and induce transparency of information, it is suggested that social enterprises provide certain mandatory disclosures to investors and the SSE viz. list of ongoing social sector projects, strategic goals and objectives, statement of purpose, business model details, annual and interim audited financial statements, social impact assessment score, utilisation certificates (wherever applicable) and other due diligence related documents as deemed fit.

Appendix 2:

About NGO-Darpan portal

NGO-Darpan is a free-of-cost forum offered by the NITI Aayog in association with the National Informatics Centre to forge partnerships between the government and development sector organisations. NGOs and VOs have to get themselves enrolled on the portal to obtain

a unique ID before they can be listed in the portal or can ask for grants. In a way, NGO-Darpan acts almost as a precursor to the proposed model of an Indian SSE. The key characteristics are below.

Parameters	Details
Who can Register?	NGO or VO registered as a society, trust, non-profit company is eligible to get registered. They generally encompass organisations engaged in public service – these include charitable or support organisations, networks or federations of such organisations and professional membership associations
Characteristics of registered entities	Organisations are primarily private entities (non-government); are social enterprises and therefore do not generate profits or financial returns; are registered organisations with clearly defined objectives in the social sector
State level support	Central ministries and departments have been advised to appoint state level intermediary organisations to act on their behalf for better coordination and monitoring of NGOs and VOs; states recommend NGOs to be listed, evaluate their credentials and undertake field verification of the projects undertaken by NGOs and VOs
Monitoring and evaluation	Third party evaluation of capability, focus, organisation capability, programme delivery of NGOs; online and on-field verification of schemes implemented through NGOs and VOs
Accountability and transparency	Grants offered to NGOs and VOs are to be reflected in Public Financial Management System (PFMS) of the Controller General of Accounts, Ministry of Finance through a dedicated NGO-Partnership system. Portals of various ministries providing the grants are linked to NGO-Darpan for transfer and transparency of records and data. In case of default, misuse of funds or cessation of existence of an NGO, there are provisions to acquire assets created by such grants
Electronic integration of data	All information regarding registered NGOs, VOs, schemes, projects sanctioned, are integrated in NGO-Darpan. The portal also has an online system for application of grants to various Ministries/Departments on various schemes and projects being implemented

NGO-Darpan provides a readymade platform with defined institutional structure that can be further enhanced to integrate the proposed features of an SSE. This would eliminate the need for conceptualising and designing a

new platform from scratch and would also reduce the time on formulating a process of on-boarding of social enterprises.

End notes

1. Beyond income, beyond averages, beyond today: Inequalities in human development in the 21st century, Human Development Report 2019, UNDP, accessed on 30 April 2020
2. Social sector funding - An eye on impact, SIDBI, accessed on 30 April 2020
3. How can an NGO accept international donations in India, Save the Children, June 2016
4. NGO crackdown has foreign fund inflows plunging 40% since Modi, BusinessLine, March 2019
5. What you need to know about impact investing, Global Impact Investing Network (GIN), accessed on 30 April 2020
6. The promise of impact investing in India, Brookings, July 2019
7. SVX invest for impact" website
8. Stock exchanges for social enterprises, Forbes, March 2014
9. SVX launches platform with New Issuers, businesswire, November 2017 (USD to INR conversion used as USD1=INR75 as on 6 July, 2020)
10. Impact investment Exchange: Taking wall street to the backstreet, Wealth & Society, January 2019
11. Women's Livelihood Bond- case study, IIX, February 2018
12. Sasix website, accessed on 30 April 2020
13. Social stock exchange: a market-oriented technology-based solution for impact investment and transparency in social welfare projects, Centre for Public: Public Research, May 2013 (Rand to INR conversion used as Rand 1=INR4, as on 6 July 2020)
14. The global social investment exchange (SASIX), Buckminster Fuller Institute, November 2008
15. Social Impact Investing Beyond the SIB: Evidence from the Market (GBP to INR conversion used as GBP1=INR93 as on 6 July 2020)
16. There are types of crowd-funding models viz. donation based (no financial gains expected); reward based (like donation based however special perks or benefits are provided in select cases); debt or peer-to-peer lending or P2P (used by businesses to raise capital and pay back happens in form of interest rather than equity); equity or investment (part-ownership of investors in business)
17. All you want to know about ESG funds, Businessline, March 2020
18. Impact bonds, Instiglio, assessed on 30 April 2020
19. Unpacking the impact of impact investing, Stanford social innovation review, August 2013
20. Impact investors council: capital for impact, GSG, assessed on 30 April 2020
21. KPMG in India analysis (USD to INR PPP conversion used as USD1=INR21.253 as on 22 June 2020)

Acknowledgement

Research Team:

Narayanan Ramaswamy
Madhavan Vilvarayanallur
Debabrata Ghosh
Deewakar Gupta
Supravo Palit
Sreejita Dey
Kawaljeet Kaur

Markets team

Aastha Dara
Satyam Nagwekar
Rahil Uppal



KPMG



KPMG *josh* **IT SHOWS**

**IN OUR ABILITY TO TRIUMPH OVER
ANYTHING IN OUR SPIRIT OF
UNDYING ENTHUSIASM OUR DRIVE
TO ACHIEVE THE EXTRAORDINARY
UNMOVED BY FEAR OR CONSTRAINT
WE'RE DRIVEN BY JOSH AND IT SHOWS**

KPMG in India contacts:

Narayanan Ramaswamy

Partner and Head

Education and Skill Development

T: +91 98400 78242

E: narayananr@kpmg.com

Madhavan Vilvarayanallur

Partner

Education and Skill Development

T: +91 97910 39872

E: vmadhavan@kpmg.com

Debabrata Ghosh

Director

Education and Skill Development

T: +91 98919 06053

E: debabrata@kpmg.com

home.kpmg/in



Follow us on:

home.kpmg/in/socialmedia



The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2020 KPMG, an Indian Registered Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved.

The KPMG name and logo are registered trademarks or trademarks of KPMG International.

This document is meant for e-communications only. (026_THL0720_RU)