ROLE OF THE SOCIAL STOCK EXCHANGE IN INDIAN CONTEXT

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Abstract: India’s economic imperative is to feed, clothe, educate and empower more than a billion people, in ways that conserve and grow its natural, cultural and social heritages. It cannot expect to accomplish this lofty objective on the strength of conventional commercial capital alone. The proof of that is that there are around 3 million non-profit organizations. One of the major hurdle these Not for Profit Organizations (NPOs) face is the lack of financial assistance to carry on their efforts, in absence of any formal structure to raise funds. On the other side, there are people who would want to donate/invest/fund NPOs or For Profit Organizations (FPEs) carrying on programs and projects having social impact. However many of them stop short due to lack of confidence of how the funds are utilized, due to absence of any formal structure. This is where the Social Stock Exchange (SSE) would give NPOs/FPEs (For Profit Organizations) with social objective, access to donors and confidence to the Donors on the impact of their donations/contributions. Currently SSE is operating in UK, Canada, South Africa etc. geared up its investments Indian market has also profound by introduction of SSE. This proposal was initiated in The Union Budget for 2019-20 allowing investors to trade exclusively in companies with social and environmental goals.

The present paper highlights basic concepts of Social Stock Exchange and various terms associated with it, such as Social Enterprises and Impact Investment. It also analyses the functionality & probable challenges in introducing SSE in India.

Index Terms: Social Stock Exchange, Social enterprises, For Profit Enterprises, Not for Profit Organizations

I. INTRODUCTION

Indian corporations (including private and public companies), social enterprises, volunteer groups, and others collaborated during the pandemic. They gave resources to society’s most vulnerable groups, such as migrants, healthcare services to individuals living in distant locations, and financial access to women, among other things. Grants from the government or other organizations, contributions, CSR spending, and monies earned from charity events held by large corporations are the key sources of their income. The resources they have available are not enough to meet their needs. Due to this, it is imperative that these organizations have access to more funding. In essence, SSE is not only a place to list securities or other funding structures but also a set of procedures that filter out all entities that are not only creating social impact but additionally reporting that impact. The SSE will operate independently within the existing stock exchanges. SSE will not only benefit social entrepreneurs but also retail investors who wish to participate in the social sector somehow.

II. REVIEW OF LITERATURE:

Asian Development Bank (2012) in their report titled, “India Social Enterprise Landscape Report” bring to light that social enterprises have the potential to make India's spectacular growth story work better for its citizens. Through their report they aim to provide a broad overview of the S.E.s landscape in India by covering different sectors and how S.E.s will address the various social and environmental needs

Galina S., Rebehy P. et al (2013) in their paper titled “Determinants of attractiveness in Social Stock Exchange” aimed to identify a pattern of social projects which led to successful funding of projects in social stock exchanges. This was an empirical study, consisting of a sample size of 155 projects and based on data published on SSE sites across Brazil, Portugal and South Africa

Chhichhia B. (2014) in her research paper titled, "Social Stock Exchanges-Innovative Financing for international development" introduces ‘social finance’ as a term that refers to the emergence of a new market pattern characterize by a range of complex structure, instrument and players. She emphasizes that a new structure that is trending in social finance is the Social Stock Exchange which is a trading platform that allows social business to raise capital by attracting ethical investors willing to invest in business that have a dual, corporate and social mission

Dadush .S (2015) in her research paper titled "Regulating Social Finance: Can social stock exchanges meet the challenge?" highlights that social finance is fast becoming a mainstream source of funding of goods and services which target poor people across the globe. Through her research paper she aims to bring out a regulatory challenge with respect to social stock exchange which needs to be addressed.
Wendt, K. (2017) in her research paper titled “Social Stock Exchanges-Democratization of Capital Investing for Impact” stresses on redirecting investments and finance to impact oriented investments that are compatible with the U.N. Sustainable Developments Goals and the Paris Agreement which is a key factor in turning around the investment philosophy.

III. OBJECTIVES:
The study has been geared to achieve the following objectives;
1. To study the basic concepts of Social Stock Exchange and various terms associated with it
2. To study the proposal of Social Stock Exchange and how it would be helpful in Indian context
3. To study the probable challenges in introducing SSE in India

IV. RESEARCH METHODOLOGY:
Data collection method:
This study has been carried out with the help of secondary data only, all the data has been collected from the various sources such as websites & reports and compiled as said by the need of the study.

Sources of data collection:
The study is based on the published data. For the purpose of present study, the data was extracted from the various newspapers, journals, articles and websites particularly from Securities and Exchange Board of India and Ministry of Commerce. Budget speech of July 2019 has also been analyzed.

Social Stock Exchanges (SSE) are dedicated platforms that allow investors to purchase stakes in social enterprises, volunteer groups and welfare organizations. The social exchange platform is an innovative measure to involve public participation in social causes through the equity route. What a Social Stock Exchange is, two terms —social enterprises and impact investment— need to be understood.

V. SOCIAL ENTERPRISES IN INDIA – AN OVERVIEW
A social enterprise is a revenue-generating business. Its primary objective is to achieve a social objective, for example, providing healthcare or clean energy. The enterprises that create social impact can be broadly categorized into two: For-Profit Enterprises (FPEs): It include companies registered under the Companies Act, sole proprietorships, partnership firms, HUFs and limited liability partnerships. Non-Profit Social Enterprises (NPOs): It includes Section 8 companies, trusts and societies. The key difference between these two categories is that they source different kinds of capital. Specifically, FPEs can raise equity while NPOs cannot.

VI. IMPACT INVESTMENT—
The investment made into businesses with the aim to make a noticeable social, economic and environmental impact? At the same time it generates a wide range of returns, ranging from profit to publicity to creating awareness, to educating masses etc.

INTERNATIONAL SCENARIO:
The SSE concept has been around globally in many countries in various forms, each country carrying its own unique SSE features. For instance, the UK Social Stock Exchange does not facilitate raising of funds at all but rather acts as a mere connecting platform for investors and social enterprises. Other SSE’s act as a crowd-funding platform for impact investors to invest and donate into enterprises that match their investment objectives. Crowd-funding refers to the solicitation of funds from multiple investors through a web-based platform or social networking site for a specific project, business venture or a social cause.

The SEBI Consultation Paper on Crowd Funding in India, as well as the IOSCO Staff Paper on Crowd-funding: An infant industry growing fast specify four types of Crowd-funding as under:

![Figure 1: The Various Forms of Crowd-Funding Activities](image)

Social Stock Exchanges around the world mostly follow the Community Crowd-funding model. The IOSCO paper highlights that the difference between the community crowd-funding and financial return crowd-funding is that community crowd-funding does not provide any financial return in the form of a yield or a return on investment.
As per the SEBI Consultation paper Donation crowd-funding denotes solicitation of funds for social, artistic, philanthropic or other purpose, and not in exchange for anything of tangible value. For example, in the US, Kickstarter and Indiegogo are some of the platforms that support donation based crowd-funding.

On the other hand reward crowd-funding refers to solicitation of funds, wherein investors receive some existing or future tangible reward (such as an existing or future consumer product or a membership reward scheme) as consideration. Most websites that support donation based crowd-funding, also enable reward crowd-funding. For example, Kickstarter, Rockethub, etc.

However the above mentioned types do not fall within the purview of a securities market regulator in global practice, as they do not provide any financial return in the form of a yield or return on investment and is treated merely as a donation/grant.

The budget proposal called for the creation of a Social Stock Exchange under the purview of the Securities Market Regulator of India. This sparks the question of whether the Social stock exchange (which could pick up a crowd-funding model) would be a financial return crowd-funding (which provides a return on investment) or as a community based crowd-funding model merely overlooked by SEBI or as both.

VII. SOME OF THE GLOBAL SSE FRAMEWORK IS AS UNDER:

The Impact Exchange (Singapore) is based on a crowd funding model that enables mature social enterprises to raise capital by issuing securities to a broader group of investors on a public platform that will facilitate trading in listed securities on a regulated stock exchange. It provides exposure to a global base of impact investors looking for transparent and liquid investment opportunities. Social Venture Connexion (Canada) allows Private Offers from accredited investors as well as raising of funds from the general public. Kickstarter, Indiegogo, etc. (USA) as mentioned earlier, allow both social lending as well as reward crowd-funding for social enterprises.

Learning from SSE models in other countries:

India has a huge advantage in setting up its exchange: It can learn from SSEs set up in various other countries over the years, including the U.K., U.S., Canada, Singapore, Brazil and South Africa. While these countries’ SSEs are similar to India’s emerging platform in their fundamental motives and objectives, each of these models is distinctive and suited to the needs of the country’s development sector. The graphic below provides a snapshot of the key features of some of these models.

![Figure 2: Key Features of Some SSE Models, Adapted from KPMG, 2020](image)

Though many of the SSE models launched in other countries have successfully raised capital for social enterprises, some have failed too. For instance, Impact Us was established in the U.S. with financial support from the Ford Foundation, the Kellogg Foundation, the MacArthur Foundation and the Open Road Alliance, and was supposed to be a game-changer in the global impact investment industry.

The fact that it closed just a year after launching raised questions about this model, which have been echoed by similar closures of platforms like Mission Markets and Enable Impact. So, what went wrong with these efforts — and how can India’s SSE avoid their fate?

Think of it as a “chicken and egg” problem: SSE platforms need both investors and social enterprises for the arrangement to work. But a newly launched SSE platform may not create enough value to entice enterprises to sign up when there are no (or few) investors involved — and vice-versa. This highlights the need to build significant confidence among stakeholders on both sides, to persuade them of the eventual benefits, and to onboard them onto the SSE platform.

VIII. EVOLUTION IN INDIA:-

In July 2019, during the announcement of the Union Budget FY19-20, India’s Finance Minister Nirmala Sitharaman proposed a social stock exchange to help enterprises and voluntary organizations working for social welfare raise capital through debt, equity or mutual funds. “It is time to take our capital markets closer to the masses and meet various social welfare objectives related to inclusive growth and financial inclusion”, she said in parliament. The social stock exchange was proposed to be set up under the ambit of Securities Exchange Board of India (SEBI). The move was welcomed as a harbinger of greater inclusive growth and commitment to support social enterprises in India.

Following the budget announcement, SEBI has set up an expert panel in September 2019 to examine and make recommendations on the structures and mechanics of a social stock exchange. Under the chairmanship of Mr. Ishaat Hussain,
Director at SBI Foundation and former Finance Director at Tata Sons, the committee’s objective was to suggest a feasible architecture and outline recommendations for setting up an SSE mechanism in India. The panel consisted of representatives of active stakeholders in the realm of social impact investing, Finance Ministry, stock exchanges and NGOs. The working group also conducted a series of consultations with various stakeholders including voluntary organizations, social enterprises and philanthropic organizations to compile their inputs.

The working group report lays out several funding instruments such as zero-coupon-zero-principal bonds, social venture funds, and mutual funds, “providing a wide gamut of options to “donor” investors looking to invest with an objective to create a social impact. This initiative may also enable companies to be able to deploy CSR funding by connecting directly with social organizations. For example, The Cancer Fund by HDFC Mutual Fund is one example. It operates as a standard mutual fund, with the exception that the returns generated are channeled towards the financing of NPOs. Its investors get their money back from HDFC MF, but any interest or gains that are made are donated to the NPO. The group has submitted its report in April 2021.

IX. THE NEED FOR SOCIAL STOCK EXCHANGES IN INDIA:

To meet the investment demand in human development sector:

- India needs massive investments in the coming years to be able to meet the human development goals identified by global bodies like the UN.
- This can’t be done through government expenditure alone.
- Private enterprises working in the social sector also need to step up their activities.

To solve the fund crunch faced by social enterprises:

- Social enterprises are very active in India. However, they face challenges in raising funds.
- One of the biggest hurdles they face is, apparently, the lack of trust from common investors
- As per a survey conducted by Brookings India, 57 per cent of the social enterprises identify access to debt and equity as a barrier to growth and sustainability.

Transparency and accountability:

- Because of rigorous due-diligence and performance metrics that an SSE would be installing for background checks for investors.

Synergy between investor and investee in social aims:

- Canvas of choice would be much wider allowing investor and investees with similar visions and missions to connect seamlessly.

Performance-based philanthropy:

- As performance of the enterprises listed on an SSE would be closely monitored, it will result into better project implementation.

X. HOW SOCIAL STOCK EXCHANGE WILL WORK?

![Diagram of how SSE will work](image)

XI. PROPOSED MECHANISM FOR FUND-RAISING IN SSE

Social Stock Exchanges aim to effectively deploy fundraising instruments and structure available under specified guidelines. These instruments depend on the nature of social enterprise seeking funding. The instruments are different for NPOs and for-profit enterprises Instruments for non-profit social enterprises are as follows:

1. Zero coupon zero principal bonds:

Allowing NPOs to directly list on the SSE through issuance of bonds in the form of zero coupon or zero principal bonds. This is a feasible option to unlock funds from donors, philanthropic foundations and CSR spenders. These bonds would carry tenure equal to the duration of the project that is being funded, and at tenure, they would be written off the investor's books.
2. Social Venture Funds (SVF):

An SVF is a category 1 Alternative Investment Fund (AIF) that is already allowed by SEBI to issue securities or units of social ventures to investors.

3. Mutual funds:

An asset management company could offer closed-end mutual fund units to investors. The units could be redeemable in principal terms, but all of the returns could be channeled towards suitably chosen NPOs by the fund which acts as the intermediary.

4. Pay-for-success models:

Pay-for-success models through lending partners or through grants are highlighted as effective mechanisms to ensure a more efficient and accountable deployment of capital.

For for-profit social enterprises (FPEs):

1. Equity listing:

FPEs would list equity on the SSE subject to a set of listing requirements, including operating practices (financial reporting and governance) and social impact reporting.

2. Social Venture Funds (SVFs):

AIFs and SVFs already exist for FPEs but do not require social impact reporting.

XII. BENEFITS OF SOCIAL STOCK EXCHANGE:

For social enterprises:

- SSE platform will acknowledge the problems of investment fundraising for social enterprises
- There is a great opportunity to unlock funds from donors, philanthropic foundations and CSR spenders, in the form of zero-coupon zero principal bonds.
- Helps small social enterprises to gain trust among impact investors

For investors:

- SSE will bring greater transparency for social enterprises, assisting investors to better evaluate the social enterprises they would like to invest in
- Investors in zero coupon zero principal bonds may also be awarded a tax benefit

For social sector:

- SSE is a significant step towards the encouragement of an ecosystem to support the growth of social finance because it:
  - Open up avenues for direct listing and streamlining funding mechanisms for NPOs
  - Innovation of new funding instruments and funding structures

For government:

- Government gets some relief on its welfare spending, as private sector enterprises could pool in capital for investing in social sector.

For Indian society as a whole:

- Improve our performances in human development indicators
- Helps to improve India’s image on global front.

The Social Stock Exchange will be a new segment of existing stock exchanges. Non-profit enterprises and for-profit social enterprises with an explicit social intent and impact will be allowed to list on the Social Stock Exchange. These entities will be allowed to raise funds from investors through equity, Zero Coupon Zero Principal bonds, Mutual funds, social impact funds and development impact bonds. Entities that would want to raise funds via the social stock exchange will have to register with the same, SEBI said.

Under the new framework, the capital market regulator said that social venture funds will be renamed to social impact funds under SEBI AIF regulations with a minimum corpus requirement reduced to Rs 5 crore from Rs 20 crore earlier. In terms of auditing of social enterprise, SEBI said that initially only reputed auditing firms having expertise in the area of social audit will be allowed to carry out audits employing social auditors who have certification courses with the National Institute of Securities Management.

SEBI also said that it will in due course of time amend its regulations towards initial and continuous disclosures for social enterprises that will cover aspects of social and financial impact and governance.

XIII. CHALLENGES:

Given the flurry of SSEs around the globe, how should the sector coherently develop so that it achieves its intended social mission while adding real value to the societies it serves? We need a number of measures to give meaning to the SSE concept at this juncture:
Education, training, and awareness:
This applies to all market players; we need to create a common understanding of metrics and instill the right horizon mentality for all investment decisions. This would allow social businesses to attract capital and set them apart as a special “asset class” like traditional for-profit investments.

Creating social businesses:
There are efforts underway to create and support social businesses, but we need more. Many still think that three years is “the make or break” line for any new business and social businesses are especially vulnerable to failure due to lack of resources and uncontrollable environments. It is much easier to evaluate a new tech start up than a company providing vaccines to reduce mortality rates in India!

Policy and regulation:
This provides the greatest opportunity for work; governments need to assist in creating social finance markets, and then support them with the right mix of policy and legislative tools. For example, there are still legal restrictions preventing fund managers from investing in social finance in many countries, there is minimal guidance for type B-Corporations, and there are minimal or no incentives (tax or otherwise) for investors to invest in social businesses. In its leadership of the G8, the UK’s Social Impact Investment Taskforce includes seven countries, the EU, and related working groups. India should follow suit and work closely with the Task Force to craft national solutions.

Research and development:
This is another area where small investments could reap huge benefits in the future. Investors—whether local governments, philanthropic organizations, or foundations—need to provide more seed funding to understand and gauge the necessary drivers for impact investment, and boost the organizational capacity of the social sector. This knowledge would provide the right framework within which investors can make more holistic decisions that include social businesses and SSEs.

XIV. CONCLUSION:
As the Covid-19 effects on the world economy show, it is critical for public and private sources of capital to come together and develop ingenious methods to ensure that capital flow to the social sector is unhindered and capital is utilized effectively to generate a lasting impact for the community.

Institutional support through SSEs ensures that more investors are encouraged to integrate environmental aspects (such as resource conservation, environmentally sustainable working practices), social aspects (including privacy, data protection, employee welfare) and governance aspects (like board diversity, conflicts of interest resolution mechanism, independent oversight of management) into the evaluation of enterprises, moving beyond financial statements.

Building on the learning’s from both successful and unsuccessful global SSEs – while also acknowledging the Indian context – here are some key considerations for setting up an effective SSE in India:

- The platform should have a clear definition of what a qualifying social enterprise is, and standard metrics to measure the impact of a social project.
- Innovation, learning and regulation should be key drivers of the SSE’s development, but the regulator should avoid an “all at once” approach and instead continuously refine the working of the SSE as it grows.
- The SSE should create a structured strategy to onboard, screen and scale funding to impactful social enterprises.
- The platform should shift investors’ focus from seeking short-term financial returns to providing patient capital over longer time horizons.
- The SSE should build social enterprises’ ability to attract more capital by mobilizing funds from investors.

While the momentum behind the creation of an SSE represents a promising step towards building India’s impact investing ecosystem, it is just the beginning. The government must create an enabling regulatory environment for the SSE to accomplish the desired results. It should ensure minimal barriers for the on-boarding, reporting and overall functioning of social enterprises. There should be sufficient tax incentives for investors, and mechanisms to ensure a seamless flow of funds to social enterprises. Ultimately, if it is designed well, India’s SSE should be able to streamline public and private sources of capital for effective use by social enterprises – without reducing the benefits they deliver to customers at the bottom of the pyramid.

To this end, all efforts need to be directed to make sure that an enabling regulatory environment is created for the planned SSE with a minimal compliance burden imposed on the enterprises, social entrepreneurs and investors.

XV. REFERENCES:
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