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**SOCIAL ENTREPRENEURS** April 3, 2009, 3:00PM EST

**Making a Profit and a Difference**

*As the economy reels, enterprising individuals who apply business practices to solving societal problems are gaining support from public and private sectors*

By [Stacy Perman](http://www.businessweek.com/print/bios/Stacy_Perman.htm)

Social entrepreneurs—enterprising individuals who apply business practices to solving societal problems, such as pollution, poor nutrition, and poverty—are now 30,000 strong and growing, according to [B Lab](http://www.bcorporation.net/), a nonprofit organization that certifies these purpose-driven companies. Together, they represent some $40 billion in revenue.

The idea of blending a [social mission with business](http://bx.businessweek.com/social-entrepreneurship/) is not new. One of the founding forces behind the movement, the [Ashoka Foundation](http://www.ashoka.org/" \t "popup), since its inception 1981 has granted multiyear living stipends to support more than 2,000 fellows dedicated to finding answers to a host of social ills through business ventures. Indeed, the concept of building a profitable business model in which doing good is an intrinsic part of the business and not just a philanthropic sideline has been gaining ground in recent years. Sally Osberg, president and chief executive of the [Skoll Foundation](http://www.skollfoundation.org/" \t "popup) in Palo Alto, Calif., another guiding force within the social venture community, says the number of institutes, universities, and organizations that are now tapping into social entrepreneurship has mushroomed since former eBay ([EBAY](http://investing.businessweek.com/research/stocks/snapshot/snapshot.asp?symbol=EBAY)) President Jeff Skoll established the foundation in 1999.

Now, as the economy reels, both the government and the private sector are looking for inventive ways to bring back prosperity, and many are counting on these entrepreneurs as a powerful tool for change. "Social entrepreneurship correlates to this growing realization that entrepreneurs are the key to a vibrant economy and to solutions that are badly needed," says Osberg. It's not all pie in the sky, says Bo Fishback, vice-president for entrepreneurship at the [Kauffman Foundation](http://www.kauffman.org/) in Kansas City, Mo. "Many social entrepreneurs have shown they can accomplish their mission," he says. "They can deliver on the social good and report a cash flow."

Not surprising, then, that they've caught the attention of such venture capitalists as those at [Acumen Fund](http://www.acumenfund.org/), a nonprofit that invests in companies that try to alleviate poverty, and [Bay Area Equity Fund](http://www.allianceforcommunitydevelopment.org/overview.html), which backs businesses aiming to make social or environmental improvements to San Francisco's needier neighborhoods. (See these [additional resources](http://www.businessweek.com/smallbiz/content/mar2009/sb20090330_647056.htm) for entrepreneurs seeking funding sources that back social ventures.) President Obama has even suggested starting a new government agency to help socially conscious startups gain more access to venture capital.

**WHO YOU LIKE BEST**

In January, we asked readers, staffers, and members of the social venture community to nominate candidates whose trailblazing companies, in operation for at least a year, aimed to turn a profit while tackling social ills. The 200-plus nominations we received included such entrepreneurs as Alex Mittal, whose Philadelphia-based Innova Materials makes antimicrobial products for private industry, then uses revenues from these efforts to develop water purification systems for the developing world. Kirsten Tobey and Kristin Richmond, founders of Revolution Foods, deliver nutritious lunches to more than 100 schools (that's 20,000 meals a day) in low-income areas in San Francisco and Los Angeles. Rachel Sterne, another social entrepreneur, encourages those living under repressive regimes to post their own reportage at her profit-sharing Web site, Groundreport.com. You can take a look at each of the 25 ventures we profiled in our [slide show](http://images.businessweek.com/ss/09/04/0403_social_entrepreneurs/index.htm), then vote for the business you feel holds the most promise.

Some attribute social models pioneered by small outfits to the social responsibility efforts espoused by large corporations. For instance, about three years ago, Wal-Mart Stores ([WMT](http://investing.businessweek.com/research/stocks/snapshot/snapshot.asp?symbol=WMT)), the world's biggest retailer, launched a program to promote sustainability, urging its many vendors to produce ecofriendly products while encouraging its consumers to buy them. General Electric ([GE](http://investing.businessweek.com/research/stocks/snapshot/snapshot.asp?symbol=GE)) made its green mark manufacturing high-efficiency incandescent light bulbs, and such manufacturing giants as Clorox ([CLX](http://investing.businessweek.com/research/stocks/snapshot/snapshot.asp?symbol=CLX)) have begun to roll out their own lines of "green" cleaning products. In March, Cadbury ([CBY](http://investing.businessweek.com/research/stocks/snapshot/snapshot.asp?symbol=CBY)), manufacturer of England's top-selling chocolate bar, announced a deal to use 15,000 tons of Fair Trade certified cocoa from Ghana by the end of this summer for its popular Dairy Milk bar. The company said the move would improve the standard of living of thousands of Ghanaians by tripling the sales of cocoa farmers there.

One of this year's finalists, Daniel Lubetzky, founder of $25 million Peaceworks, which works as a catalyst for peace by encouraging joint snack-food ventures among people of different backgrounds in volatile regions around the world, says it is not enough to impose an artificial business model on a social issue. Lubetzky, who was awarded a $1 million grant from the Skoll Foundation in 2008, says that doing good alone will not ensure success. "I had an earlier company that totally tanked," he says. "I didn't understand the product line well, but I was passionate about the mission. The failure taught me that one can't advance a social mission if the business model doesn't sell. You can't just sell a social mission. You still have to come up with the best product with the best prices." Given the current economic climate, that rings particularly true.

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**Social innovation**

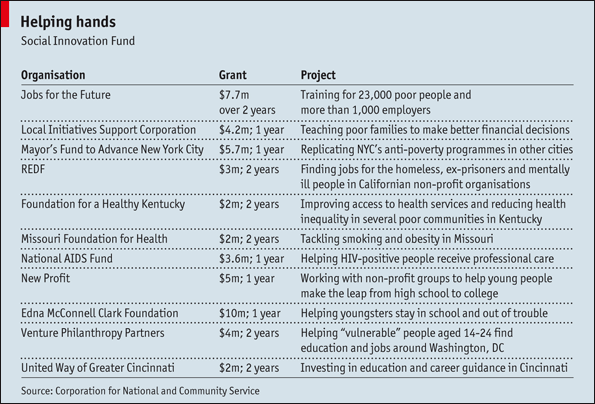
**Let's hear those ideas**

**In America and Britain governments hope that a partnership with “social entrepreneurs” can solve some of society’s most intractable problems**

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POLICYMAKERS on both sides of the Atlantic are keen on a new approach to alleviating society’s troubles. On July 22nd Barack Obama’s administration listed the first 11 investments by its new Social Innovation Fund (SIF). About $50m of public money, more than matched by $74m from philanthropic foundations, will be given to some of America’s most successful non-profit organisations, in order to expand their work in health care, in creating jobs and in supporting young people (see table).



Although the SIF accounts for a tiny fraction of the federal budget, the fund embodies an approach that the administration plans to spread throughout government. The fund is one of several efforts to promote new partnerships of government, private capital, social entrepreneurs and the public, pushed by the White House’s Office of Social Innovation and Civic Participation (OSICP), which Mr Obama created soon after taking office. These initiatives include another fund, i3 (for “investing in innovation”), in the Department of Education and cash prizes for novel answers to social problems.

Three days earlier David Cameron, Britain’s prime minister, gave a speech in Liverpool outlining his vision of a “Big Society”. At its heart, he sees a similar partnership to Mr Obama’s. A Big Society Bank will “help finance social enterprises, charities and voluntary groups through intermediaries”, which sounds very like the task of the SIF. The government, said Mr Cameron, urgently needs to “open up public services to new providers like charities, social enterprises and private companies so we get more innovation, diversity and responsiveness to public need” and to “create communities with oomph”.

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**A new name for brains and money**

“Social innovation” is the increasingly common shorthand for this approach to public-private partnerships. It differs from the fashion in the past couple of decades for contracting out the delivery of public services to businesses and non-profit groups in order to cut costs, in that it aims to do more than save a few dollars or pounds—although that is part of its attraction. The idea is to transform the way public services are provided, by tapping the ingenuity of people in the private sector, especially social entrepreneurs.

A social entrepreneur is, in essence, someone who develops an innovative answer to a social problem (for instance, a business model for helping to tackle poverty). A decade ago the term was scarcely heard; today everyone from London to Lagos wants to be one. Social-entrepreneurship conferences are invariably the best attended events for students at leading business schools.

The idea behind social entrepreneurship is that fresh, businesslike ideas will bring about a productivity miracle in the “social sector” (public services plus charity) similar to the one that began in business in the 1990s. Already, a growing number of social entrepreneurs have made a mark. The best known is probably Muhammad Yunus, the Bangladeshi founder of Grameen, a microfinance bank, and winner of a Nobel peace prize. Another prominent example is Wendy Kopp, the founder of Teach for America, which puts thousands of recent graduates from leading universities to work as teachers in some of the country’s worst schools.

However, so far the enthusiasm for social entrepreneurship has run ahead of its effects. The problem has not been a lack of good ideas (even if plenty of people who call themselves social entrepreneurs are in truth conventional charity workers). Innovative projects have ameliorated seemingly hopeless social troubles, for instance by reducing rates of reoffending by former prisoners or by helping children from the rougher parts of American cities to graduate from college.

The problem is instead one of speed and scale. Successful innovations have spread only slowly, if at all. In business, entrepreneurial firms that do well grow fast; but social entrepreneurship does not yet have a Microsoft or a Google. Policymakers hope that with encouragement from the state social entrepreneurs’ best ideas can be spread faster and wider.

Politicians’ interest in social innovation has been sharpened by the rapid deterioration of governments’ finances. Even sustaining today’s public services out of taxes alone looks impossible. Fresh ideas that promise as much, or more, for less are welcome. “The silver lining in any economic crisis is that it can force government to take necessary steps that, in more comfortable times, would fall victim to inertia,” explains New York’s mayor, Michael Bloomberg in a foreword to a new book, “The Power of Social Innovation”.

This book is a sort of bible of social innovation, full of examples of social entrepreneurs’ successes. It sets out both the potential of the partnership approach and the huge difficulties it will have to overcome. Its author, Stephen Goldsmith, is a Harvard professor, but his insights come from experience. As Republican mayor of Indianapolis, he won a reputation as a leader of a new breed of reform-minded American city bosses. His obsession with value for public money led him to fire 40% of the city’s non-uniform workers. He improved quality and cut costs by letting private firms compete with the public sector to supply many of the city’s services.

After the presidential election of 2000 he joined the administration, helping to shape George Bush’s plan to hand provision of some services to faith-based groups. He became chairman of the Corporation for National and Community Service, which now oversees the SIF.

Mr Goldsmith says that society is on the threshold of the fourth stage of how it addresses its thorniest problems. In stage one, at the start of the 20th century, caring for people was largely left to families and charities. In the second stage, marked by the welfare state in Britain and the Great Society in America, the government took on the job of ending poverty. Private efforts were largely crowded out. In stage three the state tried to foster partnerships with the private sector through competitive outsourcing, but although this sometimes made a big difference (as in Indianapolis), too often the partnerships were too prescriptive and highly focused on cost-cutting. In the fourth stage government will tap the ability of the private sector, for-profit and non-profit, to deliver “disruptive, transformative innovation”.

Now Mr Goldsmith is getting his hands dirty again: Mr Bloomberg “made me an offer I couldn’t refuse” to be New York’s deputy mayor for operations. His task is to build on the mayor’s work in social innovation, which has clearly influenced the Obama administration.

Mr Bloomberg took office in 2002 thinking he could run the city much as he had run the media company that bears his name. He even had all his senior staff sit in an open-plan office with himself in the middle. But the mayor was soon frustrated by a system hostile to innovation. So, among other things, he bypassed that system by creating the Centre for Economic Opportunity (CEO), which invests a mixture of public and philanthropic money in social entrepreneurs’ ideas to help lift people out of poverty, particularly by emphasising personal responsibility.

Projects are selected by competition. The winners get some public money—their merits having been proven to the city’s risk-averse bureaucrats. For instance, they have backed a controversial set of experiments to encourage the poor to be vaccinated or to pass exams by rewarding them with cash. The CEO, with the Mayor’s Fund to Advance New York City, received one of the first grants awarded by the SIF: $5.7m to replicate five anti-poverty programmes in seven other cities, including Memphis, Newark and Tulsa.

Indeed, the CEO inspired the SIF, says Mr Goldsmith, who influenced the SIF’s design. There is, however, a difference. New York’s scheme emphasises taking risks, with the expectation of the high failure-rate typical in a venture-capital fund. The SIF, despite its name, focuses less on risky innovation than on imitation. Its purpose is to find social innovations that have succeeded on a small scale and to help them have a far bigger impact. Officials call this “investing in what works”.

**Working out what works**

But how do you know that an innovation works? Businesses have profit; the social sector lacks a similarly simple yardstick. Often the things that are easiest to measure—say the number of people coming through the door of a community centre—tell you nothing about an activity’s effects. Finding better ways to measure the social impact of public spending is one of the goals of the OSICP, which has been working on this with the Office of Management of the Budget. Officials say progress has been made. One continuing challenge will be “to figure out what types of evaluation work at which stage of the scaling-up process”, says Sonal Shah, head of the OSICP.

Requiring private capital is another way to bring rigour: its suppliers are used to weighing up the returns from competing uses. That more than half of the money allocated in July by the SIF came from philanthropic foundations was an important vote of confidence. For similar reasons, the SIF is relying on non-profit intermediaries to scale up promising ideas. These bodies are less likely to fall foul of political pressure and risk-aversion when choosing which social entrepreneurs to back.

As well as the CEO, the fund chose Venture Philanthropy Partners and New Profit, two of the leading intermediaries created by a new generation of philanthropists. These people take a businesslike approach to giving that *The Economist* christened “philanthrocapitalism” in 2006. Both organisations invest donors’ money in a portfolio of non-profit groups. They take a close interest in the growth of these groups and measure their performance obsessively.

In building his Big Society, Mr Cameron also expects to rely on such intermediaries, of which the Big Society Bank is likely to be foremost. Indeed, in some respects Britain may be ahead of America in using public funds to drive social entrepreneurship and innovation. “Unlike America,” notes Mr Goldsmith, “Britain has benefited from a decade of deliberate thinking about how government should work with the social sector.” A new corporate form, the public-interest company, has given British social entrepreneurs greater flexibility in using the profit motive to scale up social innovations. America is starting to follow suit, with the B-corp, a hybrid of for-profit company and non-profit organisation.

Britain created a special government office to work with non-profit groups several years ago, when Tony Blair was prime minister. However, the Office of the Third Sector often seemed more concerned with giving voice to the concerns of the charity establishment than with tapping the ideas of social entrepreneurs. Whether its rebranding as the Office of Civil Society by Mr Cameron heralds a departure from such staid ways remains to be seen.

The British have also experimented with social-innovation funds. In 2000 Mr Blair established a Social Investment Taskforce, many of whose proposals to build up the private social sector were adopted. However, as Sir Ronald Cohen, a private-equity tycoon and philanthropist who led the taskforce, now concedes ruefully, “a disappointment was that the Labour government accepted policies but never implemented them as they should have done.” For instance, it did not use money in long-dormant bank accounts to capitalise a “social investment bank”. Mr Cameron has promised to use about £250m ($390m) of this to set up the Big Society Bank.

The details of what the bank will do, though, remain unclear. Sir Ronald’s plan was to use public funding to draw in lots of private capital, both for-profit and philanthropic, to scale up successful social-entrepreneurial ideas. At his taskforce’s recommendation, tax breaks were created for funds investing in poorer districts, which inspired among other things the creation of Bridges, a (for-profit) venture fund.

A potentially even more important British innovation appeared recently: the social-impact bond. This is a derivative tied to the performance of a non-profit organisation that is trying to tackle a difficult social problem—in the first instance, reducing the rate of reoffending by young prisoners. Private investors hand money to the selected organisation (including, in this case, a charity, St Giles) which then has the long-term capital to scale up its model without having to spend a lot of time raising funds. Depending on the recidivism rate, the government will pay investors in the first bond a return of 7.5-13%—or nothing, if the promised improvement is not achieved. In many ways the social-impact bond epitomises the new approach to social ills. It provides long-term funds for promising ideas; it transfers risk to private capital markets; and it costs public money only if the scheme provides specific social benefits.

Sir Ronald was a founding investor with David Blood, a business partner of Al Gore, and Stanley Fink, a big donor to Mr Cameron’s Conservative Party, in Social Finance, which aspires to become the Big Society Bank and which developed the social-impact bond. He believes that financial innovation of this sort has great potential in both rich and poor countries. “How about a social impact bond to fund literacy programmes in Africa?” he suggests.

Whether such bonds can attract enough profit-seeking money to make a real difference remains to be seen, says Geoff Mulgan, an adviser to Mr Blair who now runs the Young Foundation, a London think-tank. The money for the first bond came largely from philanthropists, who will be delighted if they make money but not too upset if they don’t. But there is not enough philanthropic capital around to create a big enough market for the bonds, so the true test is to attract for-profit capital, says Mr Mulgan. One useful change would be for regulators to make it clear to trustees of foundations and pension funds that “social-impact investments” are a legitimate asset class, says Sir Ronald.

In America the OSICP also has high hopes that government will be able to use cash prizes to encourage social innovation. Until recently, the only arms of government allowed to create such “incentive prizes” were NASA, the space agency, and DARPA, a research arm of the defence department. Legal changes pushed by the Obama administration should allow every department to do the same. The difficult bit is to define the contest precisely enough to reward genuine innovation that is truly useful—which is easier for scientific innovations than for social ones.

The OSICP also hope to ginger up social innovation through two things usually seen as more worthy than effective: open government and volunteering. The administration is releasing lots of once-restricted data, which OSICP says is allowing it to tap into the same crowdsourcing movement that gave birth to Wikipedia. And Patrick Covington, the new chief executive of the Corporation for National and Community Service, said recently that his agency would no longer judge its own performance by the number of volunteers or the hours they put in but by their effect.

Tea and company in Southwark

In Britain too, Mr Cameron has high hopes for volunteers. Participle, a business formed by two social entrepreneurs, Hilary Cottam and Charles Ledbeater, is trying to redesign the welfare state “bottom up”. A successful pilot, Southwark Circle, built social networks of helpful neighbours for old people living on their own in inner London. “We have seen that using limited resources to enable a social life has the effect of expanding the resources available; the time and talent of friends, neighbours and family can more than meet material needs,” says Ms Cottam.

**Wanted: civic entrepreneurs**

Within five years, says Ms Shah of the OSICP, the administration aims to prove the worth of the innovation-fund model, to develop good measures of performance and to have every part of the government thinking about this new approach to social innovation. Mr Cameron’s coalition government is at least as ambitious.

The biggest obstacle in both America and Britain is likely to be the inertia of the bureaucratic, rule-bound public sector. “I can think of 1,000 innovations,” said Mr Goldsmith soon after starting his new job in New York. “I have not yet had an innovative idea in any meeting that was legal.” Governments seem particularly bad at shifting money from old budgets to new ones, which is one reason why the SIF has started with a paltry $50m. Every government agency should be required to put 1% of its budget into innovation funds, argues the Centre for American Progress, a think-tank with strong ties to the Obama administration. The Young Foundation has proposed the same policy in Britain.

There are also powerful political pressures in favour of the status quo to be outmanoeuvred. For instance, America’s teaching unions have been fiercely opposed to many education innovations pushed by social entrepreneurs, including charter schools, and to the billionaire philanthrocapitalists who help finance them, such as Bill Gates and Eli Broad. There have been criticisms of the grant to New Profit because its founder, Vanessa Kirsch, once hired Michelle Obama.

Success may depend on the emergence of a subgroup of social entrepreneur that Mr Goldsmith calls “civic entrepreneurs”, who can navigate the treacherous waters of bureaucracy. Candidates should apply for a government job at once.