

08-103

**The Future of Social
Enterprise
Harvard Business School
Working Paper**

**V. Kasturi Rangan
Herman B. Leonard
Susan McDonald**

Copyright © 2008 by V. Kasturi Rangan, Herman B. Leonard, Susan McDonald

Working papers are in draft form. This working paper is distributed for purposes of comment and discussion only. It may not be reproduced without permission of the copyright holder. Copies of working papers are available from the author.

The Future of Social Enterprise

Harvard Business School Working Paper

V. Kasturi Rangan

Herman B. Leonard

Susan McDonald

The Future of Social Enterprise

Harvard Business School Working Paper

V. Kasturi Rangan, Herman B. Leonard, and Susan McDonald

The Future of Social Enterprise considers the confluence of forces that is shaping the field of social enterprise, changing the way that funders, practitioners, scholars, and organizations measure performance. We trace a growing pool of potential funding sources to solve social problems, much of it stemming from an intergenerational transfer of wealth and new wealth from financial and high-tech entrepreneurs. We examine how these organizations can best access the untapped resources by demonstrating mission performance and then propose three potential scenarios for how this sector might evolve:

Consolidation: In this scenario, funding will keep growing in a gradual, linear fashion and organizations will compete for resources by demonstrating performance. The sector will consolidate, with some efficient organizations gaining scale, some merging and then growing, and some failing to achieve either scale or efficiency and eventually shutting down.

Entrepreneurial: In a more optimistic future, existing and new enterprises will apply strategies to achieve and demonstrate performance, improving efficiency and effectiveness and attracting new funding sources. More organizations will enter a reformed, competitive field of social change with new entrepreneurial models, established traditional organizations, and innovative funding strategies fueling widespread success.

Expressive: Rather than focusing exclusively on performance, funders and organizations may view their investment as an expressive civic activity. As much value is placed on participating in a cause as on employing concrete measures of impact or efficiency. In this scenario, funding will flow as social entrepreneurs experiment with new models based on a range of individual priorities and relationships.

I. Background on the Social Enterprise Colloquium

Harvard Business School (HBS) founded the Social Enterprise Initiative (SEI) in 1993 to inspire, educate, and support current and emerging leaders across all sectors in applying management skills to create social value. To achieve this mission, SEI has taken an integrated approach to social enterprise research, curriculum enrichment, career development, and community engagement activities. HBS also made a deliberate decision to interpret the program to include the study of enterprises and organizations engaged in social value creation, regardless of their for-profit or nonprofit status. With this approach in mind, SEI has grown significantly in many areas since those early days.

The 2008 Future of Social Enterprise Centennial Colloquium is part of a series of activities to celebrate the HBS Centennial. It is also the most recent of several research forums and conferences that SEI has convened over the years to bring together thought leaders to advance the knowledge and practice of managing social enterprises globally. An earlier gathering resulted in a series of articles, presented in two journal volumes, aimed at building a nuanced strategy framework that would be appropriate and applicable for mission-driven organizations.¹ Business leadership in the social sector was the focus of a significant earlier event,² while a later conference produced a series of articles, collected within a book, which provided insights into how businesses can focus on the Base of the Pyramid (BoP) (i.e., low-income populations) to create win-win solutions for shareholders as well as for the global poor being served.³ A conference addressing the challenges and opportunities facing managers and leaders of large urban school districts contributed to the publication of a course book of cases on management and leadership in public education.⁴

II. Foment and Ferment in Social Enterprise

The March 2008 HBS Future of Social Enterprise Centennial Colloquium convened at a most opportune time, as the social enterprise field undergoes several major transformations. Panelists and participants examined major cross-cutting themes surrounding the future of social enterprise, including philanthropic funding flows, organizational capacity, and management strategies for impact.

Philanthropic resources are growing. In the U.S., many foundations sport enormous endowments while foundations overall now number more than 71,000, an increase of 77 percent between

¹ *Nonprofit Management & Leadership*, Vol. 11, No. 3, Spring 2001. *Nonprofit and Voluntary Sector Quarterly*, Vol. 29, No. 1, Supplement 2000.

² Kanter, Rosabeth M. *Business Leadership in the Social Sector*. Social Enterprise Video Series. Harvard Business School Publishing, 1998.

³ Conference on Global Poverty, Harvard University. Rangan, V. Kasturi, John A. Quelch, Gustavo Herrero, and Brooke Barton, eds. *Business Solutions for the Global Poor: Creating Social and Economic Value*. John Wiley & Sons, Inc., 2007.

⁴ Childress, Stacey, Richard F. Elmore, Allen S. Grossman, and Susan Moore Johnson, eds. *Managing School Districts for High Performance: Cases in Public Education Leadership*. Harvard Education Press, 2007.

1995 and 2005.⁵ Over the next 50 years, an intergenerational transfer of wealth is expected to occur between elderly adults and aging baby boomers and their families, with an estimated \$6 trillion projected to go directly to charitable causes.⁶ These resources in search of a cause frequently require proof of concrete social returns, especially given that many new donors are adopting a high-impact, entrepreneurial approach to their giving.

Likewise, the social sector is growing. Currently, more than 1.4 million nonprofit organizations in the U.S. generate \$1.36 trillion in revenue, constituting at least 5 percent of GDP, while individual charitable giving alone has reached a high of \$300 billion.⁷ As frequently noted, the sector itself is expanding to include not only traditional nonprofit organizations but also many for-profit and hybrid entities operating with strong social missions. The current blurring of boundaries among sectors⁸ means that nonprofits now routinely engage in profit-seeking activities, for-profits aggressively seek social value through business and charitable activities, and public agencies form partnerships with both – all with the goal of reducing social harms and advancing public benefits.

As the traditional nonprofit sector broadens to include a range of social enterprise models, the social sector faces three major transformations:

- Changes in the flow of funds, due to commercial activity by socially minded organizations as well as growing philanthropic sources, especially the vast sums of anticipated intergenerational wealth transfer and new wealth from financial and high-tech entrepreneurs
- A shift in the role of government, both in terms of responsibility and distribution of resources, as traditional models of grant funding give way to market competition in

⁵ The Foundation Center 2008, National Growth Trends, Number of Grantmaking Foundations by Type, accessed online at http://foundationcenter.org/findfunders/statistics/gm_growth.html, June 2008.

⁶ Havens, John J. and Paul G. Schervish. “Why the \$41 Trillion Wealth Transfer Estimate Is Still Valid: A Review of Challenges and Questions.” Boston College, January 27, 2003. Published online by the Planned Giving Design Center at <http://www.pgdc.com/usa/item/?itemID=62901&g11n.enc=ISO-8859-1>. Accessed November 20, 2007. In 1998 dollars.

⁷ Wing, Kennard T., Thomas H. Pollak, and Amy Blackwood. *The Nonprofit Almanac 2008*. Urban Institute Press.

⁸ Austin, James E., Roberto Gutiérrez, Enrique Ogliastri, and Ezequiel Reficco. “Capitalizing on Convergence.” *Stanford Social Innovation Review*. Winter 2007. Also, Wei-Skillern, Jane C., James E. Austin, Herman B. Leonard, and Howard H. Stevenson. *Entrepreneurship in the Social Sector*, Sage Publications, Inc., 2007.

which nonprofit and for-profit entities compete for government contracts and consumer subsidies

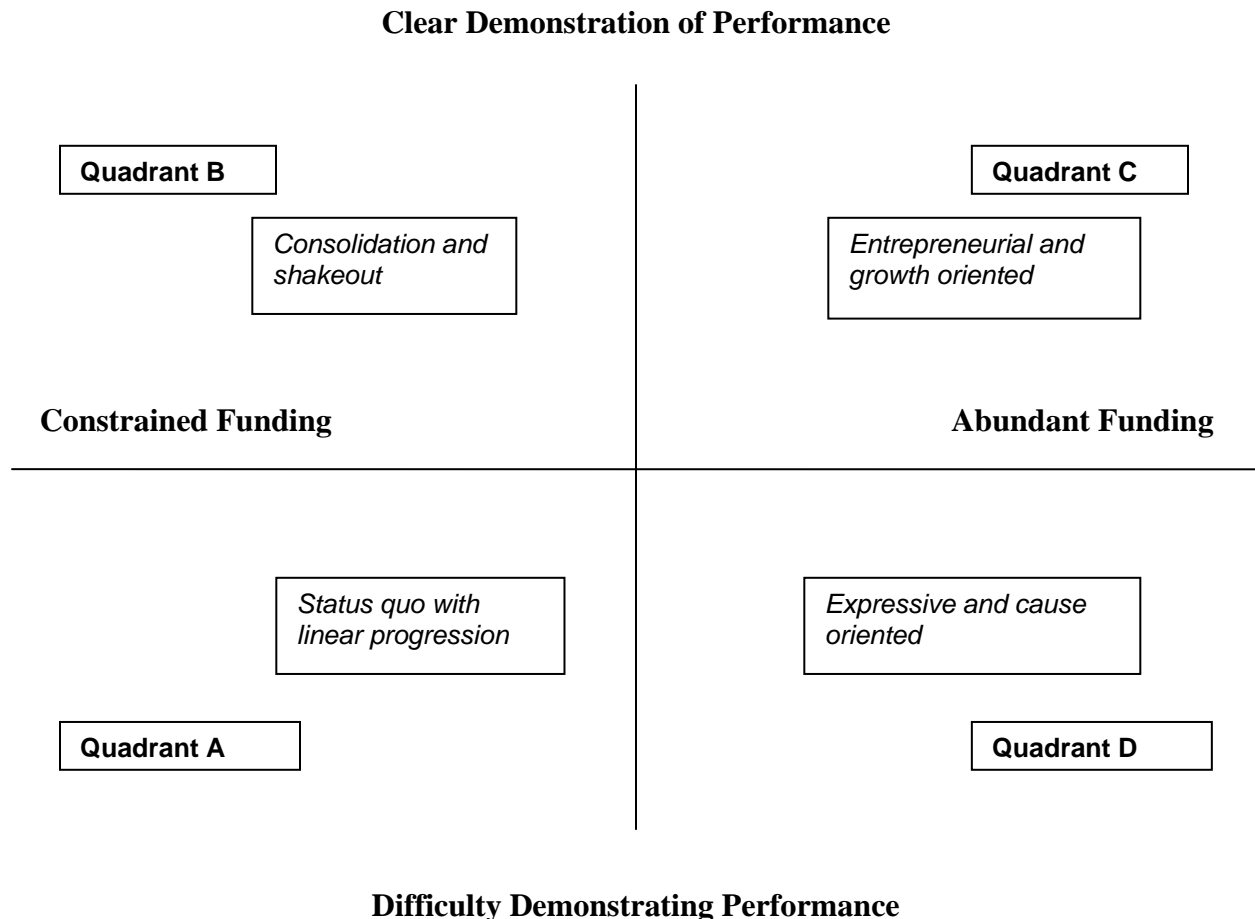
- A transformation of ideas on how to allocate resources and what results to expect as philanthropy is increasingly viewed as a social “investment,” especially as more potential funders with entrepreneurial backgrounds enter the philanthropic market

In the face of these challenges, the functional questions for nonprofit leaders and social entrepreneurs are how to acquire resources, how to build successful organizations, and how to achieve impact – and for those actors and intermediaries who support the sector with funding and expertise, how to advance all three goals. In response to these questions, the social enterprise literature is awash with claims of groundbreaking innovation, from venture philanthropy to corporate social responsibility, which offer the equivalent of philanthropic “silver bullets.” Data trends, however, suggest a somewhat different story, one of steady but not remarkable growth influenced by major demographic and political changes, and accompanied by a wealth of new models whose potential has not yet been fully explored. In fact, many innovative approaches and models that have emerged over the last 10 years remain in their infancy and await a “quantum” push to exhibit widespread benefit.

III. Future Scenarios in Social Enterprise

Given the apparent challenges and opportunities in designing, funding, staffing, and measuring social change organizations, what does the future hold for this sector? Among a broad range of possibilities, several distinct scenarios may emerge from the current transition occurring within social enterprise. These possibilities are mapped out visually below, and then each one is explored briefly. The degree to which social enterprise organizations can achieve, measure, and communicate performance is located on the vertical axis, while the amount of funding they can attract is located on the horizontal axis.

The Relationship Between Demonstrable Performance and Funding Growth



A. Status Quo: Quadrant A represents a linear extrapolation of the existing situation in which traditional nonprofit groups strive to demonstrate performance and access adequate funding to support mission fulfillment. Many of the current nonprofits are located within this quadrant. While some organizations with appealing mission and fulfillment strategies have received abundant funding, overall trends suggest that achieving and demonstrating performance is harder than it seems and that funding resources are equally hard to come by. The irony is that the sector with a potential abundance of funding may still be struggling to break out of the rut. While many new organizations are founded, few achieve scale, funding flows do not correlate with performance, and the top tier of established nonprofits retains its supremacy. Furthermore, the number of charitable foundations is growing somewhat faster than the number of charities.

Although new money lurks in the wings seeking worthy recipients, most nonprofits still find that establishing a reliable funding flow is a major challenge. This could explain why the sector may take a significant shift toward quadrant B or C.

B. Consolidation: In this scenario, funding continues to grow in a linear fashion as in the past, but with funders demanding performance, either in terms of efficiency measures or effectiveness. If many organizations fail to achieve and demonstrate performance, funding will be bottlenecked or concentrated in a small number of more efficient, typically larger organizations. The sector will consolidate, following a business model of mergers and acquisitions. As a result, organizations will increasingly compete for funding and staff, with the victor being the most efficient organization, and the losers going out of business or being absorbed. Indeed, “bankruptcy or irrelevancy is a likely path for not-for-profit organizations . . . that do not reshape themselves to achieve greater impact, efficiency, and accountability in an increasingly global, competitive environment.”⁹ In this scenario, increased emphasis will be placed on intellectual capital or on new philanthropic models to achieve results. Funding intermediaries are likely to emerge whose roles will differ from those of foundations, due to their approach toward measuring performance.

C. Entrepreneurial: In a more optimistic future, existing and new nonprofits will apply strategies to achieve impact, establish networks and partnerships, and improve both efficiency and effectiveness, thereby creating a reformed social sector. The increased demand for effectiveness could shake loose new resources as funders begin to spend their endowments and as funders and nonprofit groups collaborate on joint-venture philanthropy.¹⁰ If organizations can successfully achieve and demonstrate high performance, then new sources of funding will flow and the sector will expand, requiring increased attention to issues of leadership and management. The limiting

⁹ Lindenberg, Marc. “Are We at the Cutting Edge or the Blunt Edge? Improving NGO Organizational Performance with Private and Public Sector Management Frameworks,” *Nonprofit Management & Leadership*, Vol. 11, No. 3, Spring 2001.

¹⁰ Fulton, Katherine and Andrew Blau. *Looking Out for the Future: An Orientation for Twenty-first Century Philanthropists*. Global Business Network and the Monitor Institute. Accessed online at www.futureofphilanthropy.org, December 2007.

agent then becomes human capital as organizations seeking scale compete for star talent.¹¹ Such talent is likely to become more widely available, however, as new funding sources support competitive compensation and help build stronger organizations.

In this scenario, funding grows rapidly and social-sector activity shifts to Quadrant C, with widespread growth based on performance and encompassing both nonprofit and for-profit social mission activity. More organizations will enter a competitively structured field of social change, with new entrepreneurial models, established traditional organizations, and innovative funding strategies fueling widespread growth and success. Under this scenario, the winners may not necessarily be the larger organizations, as smaller and midsize enterprises will co-exist with larger organizations. Those addressing complex social issues will be measured on the reach and efficiency of their operations, while those addressing focused causes will be measured on the effectiveness of their interventions.

*D. Expressive:*¹² Rather than focusing exclusively on performance, funders and organizations may view their investment as an expressive civic activity and thus sector growth will not occur as much along the performance dimension (i.e., the Y-axis in our diagram). In this scenario, as much value is placed on participating in a cause as on employing concrete measures of impact or efficiency. Funding will flow as social entrepreneurs experiment with new models based on a range of individual priorities and relationships. In this case, the sector – both nonprofit and for-profit – will tend to play an expressive role, reflecting the interests of funders rather than larger partnerships of interests among funders, practitioners, and constituents.

In several of these scenarios, primarily B and C, a broad view of performance is critical. For organizations operating in the social sphere, success or effectiveness relies on a host of measures related to actual social impact (solving or reducing a larger social problem) or to more direct measures of outcomes, outputs, or simple efficiency providing services with donor dollars. In any of these cases, performance measurement should take a nuanced approach, contingent upon

¹¹ Tierney, Thomas J. “The Nonprofit Sector’s Leadership Deficit.” March 2008 white paper, The Bridgespan Group, accessed online at http://www.bridgespan.org/kno_articles_leadershipdeficit.html.

¹² Frumkin, Peter and Alice Andre-Clark. “When Missions, Markets, and Politics Collide: Values and Strategy in the Nonprofit Human Services.” *Nonprofit and Volunteer Sector Quarterly*, Vol. 29, No. 1, Supplement 2000.

the specific role that the organization plays within the broader spectrum of solving the problem. Regardless of scenario, this will require an evolution in how managers approach evaluation. While social mission groups are familiar with the challenges of attracting funding and talent, it seems that something more complex is actually occurring in the field: not a funding or talent deficit, but an imagination deficit. Social enterprise leaders need to be more visionary in their planning and strategic in their implementation to pursue the scenario they prefer.

For nonprofit and organization executives, this may include forming proactive networks and developing strategic partners; engaging donors in joint problem solving, especially related to performance evaluation; tapping new talent pools; and finding ways to incorporate performance measurement as part of organizational learning rather than as an auditing function. Funding organizations likewise must work with nonprofits and their clients across sub-sectors to develop appropriate performance measures, fund capacity and evaluation efforts, and engage with other donors on performance issues. Nonprofit boards and emerging intermediary organizations can play a catalytic role. The former can engage in strategic planning, include client representation on the board, and engage in the performance review process, while the latter can play a role in coordinating donors, establishing performance parameters, and sharing best practices.

Significant changes are occurring in the field of social enterprise, including major developments in the flow of funding, growing but often untapped philanthropic resources, and a shift in the role of government, as well as new social investment models and impact measurement tools. All of these phenomena are occurring against a larger backdrop of demographic and market change as boundaries blur among the traditional nonprofit, for-profit, and public-sector silos. Currently, the sector remains on the brink of several possible futures, including consolidation, entrepreneurial growth, and expressive experimentation. The scenario that unfolds over the next 20 years will depend largely on the ability of social enterprise leaders to make a leap forward in thought and action to capitalize on the abundant potential for social change.