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Solution Proposal

Funding – Achilles’ heel of Social Enterprises

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The social entrepreneurship model fundamentally calls into question the traditional assumption that the role of the market is to create value, while the state and civil society are responsible for redistribution and social concerns. By no means, however, is social entrepreneurship in opposition to our existing economic system − on the contrary: Successful examples of social businesses offer an approach that is rooted in the market economy, in the best sense of the word, and enrich philanthropic and governmental solutions to social problems. They fill a need that existing systems cannot. Social entrepreneurship is capable of triggering flexible, creative change and mobilizing new forces, ideas and resources, making it an agent of transformation in the interest of systemic innovation. By demonstrating that there is not necessarily a conflict between the creation of social value and economic performance, social entrepreneurship provides guidance and opportunities for generating new role models, models that are often missing in society and the business community.

In many cases, however, there is still a lack of the financial instruments and targeted support structures needed to create a solid and sustainable financial basis for the development of social businesses. While the Anglo-Saxon countries and Italy, for example, have already established the necessary legal and financial conditions for social business entrepreneurship, other countries − and not only Germany − have barely begun to do so.

Because of their social focus, social enterprises have only limited access to conventional funding. On the other hand, they can access other sources that are not available to traditional businesses. Funding for social enterprises needs to reflect the hybrid nature of social entrepreneurship organizations, but also the fact that the logic behind investment decisions in the area of social business is fundamentally different from the rationale for the investments of for-profit companies: In addition to seeking to make a profit, social investors must strive to maximize “social yield” in a systemic sense − and investees expect them to do so.

This, indeed, is the Achilles’ heel of this still-young sector: No uniform criteria have yet been established for evaluating successes and impacts; there is no social reporting standard that addresses the special nature of social business as well as the need to provide information to social investors. Many social enterprises still lack experience with scaling up or down, and have not yet developed a proof of concept for their business ideas. Moreover, funding instruments must be adapted to suit these new kinds of business models and specific social enterprises.

This is where funding from such sources as venture philanthropy and high-engagement philanthropy comes in. These sources of funding apply the venture capital approach to the social business sector, and they not only provide financial support (particularly during the startup phase), but also promote customized capacity building. Other trend-setting approaches to funding social enterprises might include the Social Impact Bonds in the UK (the effective interest earned by private investors depends on public savings achieved through the activities of their investees; if defined targets are met, public authorities repay the capital plus interest) or Germany's Social Venture Fund (specializing in professional consulting and private funding for the expansion of social enterprises).

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