

innovations

TECHNOLOGY | GOVERNANCE | GLOBALIZATION

Special Edition for the World Economic Forum Annual Meeting 2009

Social Innovation in a Post-Crisis World

Lead Essays

Social Innovation in a Post-Crisis World Klaus Schwab & Hilde Schwab

Social Ventures as Learning Laboratories J. Gregory Dees

Macro Impact on Microfinance Roshaneh Zafar

A Bank as Courageous Investor Ellen Seidman & Ron Grzywinski

The Upside of the Downturn Peter Blom

Cases Authored by Innovators

Power Play Rory Stear and Kristine Pearson

Ending Dependency Cosmas Okoli

Empowering the Rural Poor to Develop Themselves Bunker Roy

Garden in the Desert Ibrahim and Helmy Abouleish

From Fear to Hope Karen Tse

Perspective on Policy

The Resilience Imperative Philip Auerwald and Debra van Opstal

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About *Innovations*

Innovations is about entrepreneurial solutions to global challenges.

The journal features cases authored by exceptional innovators; commentary and research from leading academics; and essays from globally recognized executives and political leaders. The journal is jointly hosted at George Mason University's School of Public Policy, Harvard's Kennedy School of Government, and MIT's Legatum Center for Development and Entrepreneurship.

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Social Ventures as Learning Laboratories

We have seen that the function of entrepreneurs is to reform or revolutionize the pattern of production...

—Joseph A. Schumpeter, *Capitalism, Socialism, and Democracy*

If ever the world needed new patterns of production, it certainly does now—during the worst financial downturn in decades. Innovations, developed and tested by entrepreneurs, will help us respond to the challenges of the crisis and move into a new era of prosperity.

Entrepreneurship is part of the solution to the crisis, but, ironically, it was also part of the problem. Capital market innovations, such as interest-only adjustable rate mortgages and credit default swaps, helped to revolutionize the pattern of production in credit markets, resulting in permanent damage. Innovation can be risky business, especially if the innovators and early adopters are focused only on what is likely to be profitable for them in the short term. These capital market innovations present a worst-case version of Schumpeter's idea of "creative destruction." In this case, the harm from the destruction exceeded the value of the creation. That is not the kind of entrepreneurship we need more of.

What we need now is entrepreneurship that creates greater long-term value while drawing on fewer resources and generating fewer destructive consequences. We need business entrepreneurs whose innovations will jump-start the economy, create jobs, and cause minimal disruption. We need more of the non-destructive creation that Columbia professor Amar Bhidé has written about.¹ We also need more social entrepreneurship.

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RECOGNIZING THAT SOCIAL PROBLEMS ARE MORE PRESSING THEN EVER

Nowhere is this kind of value-creating innovation more important than in our efforts to tackle pressing social and environmental problems. This is where social entrepreneurs come in. They reform or revolutionize the patterns for addressing social issues. They measure their success in social impact. Social entrepreneurship has not gotten as much attention as business entrepreneurship and is not as well supported, but it is extremely important to the quality of our lives on this planet. It is particularly important in times like these, where financial pressures are likely to make social problems worse. As economies shrink or, in the best cases, grow much more slowly than previously expected, we can anticipate increases in poverty and unemployment.

This will exacerbate the many problems associated with poverty. Fewer people will receive adequate health care. Because of the financial burden that formal education can place on parents, fewer children will attend school. Tensions and violence may increase as the poor compete for jobs and income opportunities, as they did recently on the border of Zimbabwe and South Africa. Progress will be lost, as families that have been successful in moving out of poverty fall back into it. Though carbon emissions should decline with declining economic activity (though the dropping price of oil complicates matters), any decline is unlikely to make an appreciable dent in the growing problem of global warming. As government, business, and household budgets tighten, costly environmental protection and clean-up efforts are in jeopardy. With declining oil prices, the economics of alternative energy may become less attractive.

Because many social and environment issues are time sensitive, failure to recognize the importance of social entrepreneurship and provide adequate support for such efforts during this downturn would be a serious mistake. Damage will be done that cannot easily be undone. Social entrepreneurship is not a luxury that can be suspended while we wait for the economy to turn around.

FOSTERING A VIBRANT SOCIAL LEARNING LABORATORY

Social entrepreneurs offer us a learning laboratory: they develop and test innovative solutions to social problems. As with any form of innovation, it is impossible to know in advance what will work. This is especially true when “working” involves reducing or solving a social problem. Only by fostering a wide range of experiments can we hope to find which proposed solutions are viable, cost-effective, and scalable. This is the beauty of the small, new, resourceful ventures that social entrepreneurs tend to create. As Stanford economist Nathan Rosenberg and his co-author L. E. Birdzell, Jr., have argued, “New enterprises are useful devices for experimenting with innovation, because they can be established on a small, experimental scale at relatively low cost and therefore in large numbers, and their efforts can be intensely focused on a single target.”² Independent social entrepreneurs have

greater flexibility to experiment, uninhibited by the biases, standard operating procedures, bureaucracy, cultures, strategic commitments, and other rigidities common in established organizations of all kinds.

Because of their local knowledge and motivation to find solutions to social problems, social entrepreneurs see and construct opportunities that governments, corporations, and profit-seeking business entrepreneurs miss. Consider 2006 Nobel Peace Prize winners Muhammad Yunus and Grameen Bank. When Yunus conceived the idea of Grameen Bank, with its focus on micro-credit and its cost-effective peer-group business model, he was driven by the desire to alleviate poverty. The Bangladeshi government, the banks, the international relief agencies, and local business entrepreneurs did not see this as an opportunity. Yet, microfinance has grown to be a business that now attracts mainstream banks

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and profit-seeking business entrepreneurs. The business opportunities in microfinance were neglected until social entrepreneurs, such as Yunus and the other pioneers of microfinance, spent decades demonstrating its viability as a market. Grameen has been free from outside funding for over a decade while serving millions of customers in Bangladesh and inspiring replications around the world. Only now are markets responding to this opportunity.

PROMOTING RESOURCEFULNESS AND CREATIVE BUSINESS MODELS

As a matter of necessity, entrepreneurs, social or otherwise, have to be resourceful. They become quite skilled at doing more with less and at attracting other people's resources to their ventures, directly or through partnerships. This resourcefulness is reflected in their creative and pragmatic approach to business model design, as illustrated by Grameen's use of borrower peer groups and its very low-cost structure.

It is useful to think of social venture business models as running along a spectrum, from fully reliant on philanthropy and government subsidy at one end to fully commercial at the other. In recent years, many social entrepreneurs have been driving toward the commercial end of that spectrum to reduce their dependence

on philanthropic or governmental subsidies. Commercial strategies are not optimal for all social ventures. The business model has to align with the strategy for social impact, but when possible, social entrepreneurs do work to create sustainable, scalable ventures. For-profit ventures, social business ventures, and hybrid ventures that mix elements from the philanthropic and commercial worlds have become common.

For instance, Water Health International is a for-profit social venture that combines an innovative, relatively low-cost technology for water purification in rural areas of developing countries with an innovative business model in which villages finance the purchase of the equipment and the villagers pay a small fee for the clean water they use. VisionSpring is a nonprofit example of creative business model development. It provides low-cost reading glasses, a productivity-enhancing product, by buying the glasses produced in China and selling them through micro-franchisees, who live in the villages of the countries where it does business. Thus, it provides affordable glasses and creates income opportunities for its vision entrepreneurs.

The emergence of for-profit social ventures and the increase in nonprofits generating earned income are controversial, but this kind of experimentation is essential if we are to find ways to improve the productivity of the scarce resources we devote to social problems. When it works (i.e. aligns with social impact), it leads to a more effective allocation of scarce philanthropic and government funds. These subsidies can be freed up to flow to the organizations and causes that need them most. Through creativity in business model development, social entrepreneurs are crafting more sustainable and scalable innovations.

SCALING IMPACT AND SHARING KNOWLEDGE

While it is essential to support the early-stage innovations that make up the “learning laboratory” of social entrepreneurship, the real value comes in what society does with the results of that learning laboratory. Value is created when successful innovations are identified and then scaled or replicated to maximize their impact. It is important to note, however, that not every successful social innovation (successful in the sense of achieving its intended social impact) is amenable to scaling or replication. Local successes sometimes depend on rare conditions, scarce skills, or inefficient business models. Innovations need to be evaluated not just on their social impact, but also on their transferability and cost-effectiveness, and on the organization’s readiness for a scaling or replication effort. However, with the right kind of rigorous due diligence, key resource providers (particularly philanthropists, social investors, potential corporate partners, and government funders) can identify viable candidates for scale or replication and provide the support they need to achieve widespread impact. In a time of financial crisis, this disciplined approach is even more important. It may be hard to pick a few “winners” for

major investment, since everyone is well intentioned, but it is essential to capture the value of the experimentation.

The second way to reap value from this learning laboratory is to harvest the lessons from both the successes (scalable or not) and the failures and to share this knowledge with those who can put it to good use. Tremendous waste occurs in the social sector when knowledge is not captured and shared effectively. No one likes to admit failure, and few are willing to open their failures to inspection. Even the successes are rarely analyzed in a critical way that can contribute to a common body of knowledge. However, the learning laboratory is more likely to yield effective scalable innovations in the future if the players in the laboratory know enough not to repeat past failures and can find ways to build on past successes. This is a role for universities, consultants, associations, think tanks, and journals, such as *Innovations*.

TAKING SOCIAL ENTREPRENEURSHIP SERIOUSLY

The current financial crisis will force us to be smart about our investments in social change. This could be a healthy development for social entrepreneurship, provided that philanthropists, social investors, governments, corporations, and other key players actively foster a vibrant learning laboratory of social entrepreneurs, assess the results of these experiments, support the scaling or replication of high-leverage ventures (those that promise greater social impact per unit of financial investment), and collaborate with efforts to capture and share knowledge along the way. Leaders in any society have much to gain from taking the concept of social entrepreneurship seriously and providing social entrepreneurs with the same kind of disciplined strategic support that they provide for innovation in business.

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1. See Amar Bhidé, *The Venturesome Economy: How Innovation Sustains Prosperity in a More Connected World* (Princeton University Press: Princeton, 2008), especially Chapter 13.
 2. See Nathan Rosenberg and L. E. Birdzell, Jr., *How the West Grew Rich* (Basic Books: New York, 1986), p. 276.

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