

An economic perspective on social entrepreneurship: Insights and policy implications

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Abstract

Social entrepreneurship has an economic impact through its social purpose and the development and implementation of innovative business models that address social and environmental challenges. This chapter discusses the economic returns of social entrepreneurship through knowledge spillovers and standard-setting perspectives. Knowledge spillovers to for-profit businesses or other organizations are a critical second-order effect of social entrepreneurship. Moreover, socially motivated businesses that implement welfare-enhancing business practices also impact norms and set standards that other organizations adopt. These factors affect social entrepreneurs' overall societal and economic impact, role in competitive markets, and innovation. Overall, the review of insights on the economic returns of social entrepreneurship shows that their impact often goes beyond the specific social purpose of their business and that they play a fundamental role in the diffusion of innovative business practices. However, social entrepreneurship also has significant challenges regarding classical hurdles such as financing constraints and bureaucracy. In addition, the success and impact of social entrepreneurs may, to a larger extent, depend on founders' social and business networks, political connections, and non-conventional funding sources. These properties of social entrepreneurship, alongside their intrinsic characteristics, stress the need to develop and implement ecosystems and policy designs that account for social entrepreneurship's direct and indirect effects.

1. The relevance of social entrepreneurship

Growing social problems and the awareness of the tensions and conflicts they bring draw attention to social entrepreneurship. Social entrepreneurs' fundamental objective is to tackle social concerns through their business activity, particularly in areas where governments and philanthropy fail to sufficiently address these problems¹.

A social enterprise can be defined as an organization whose primary purpose is to generate social benefits². Social entrepreneurship creates impact from prosocial behavior through beneficial outcomes for targeted individuals, a broader community of individuals, organizations, or the environment³. This implies that private benefits for the entrepreneur, shareholders, or investors are of subordinate importance.

The term 'social' implies that the business generates positive impacts for society beyond the benefits for the entrepreneurs and employees. These broader effects can be referred to as positive externalities. Positive externalities are present when the economic activity of the social business creates a value spillover that lies beyond the objective function of the entrepreneur⁴, i.e., it creates returns to society that the entrepreneur or investors are not financially compensated for. This definition does not mean that social enterprises cannot or should not be economically viable as for-profit entities⁵. In economic terms, what distinguishes social entrepreneurship from 'regular' entrepreneurship is that in the case of social entrepreneurship, we do not assume that the beneficiaries of the product or service can or need to pay for the value being provided. Moreover, the entrepreneurs' main motivation is not driven by the need to make money from the beneficiaries but to create value rather than capture value⁶.

Thus, from a traditional welfare perspective, where the return to economic activity is the sum of consumer and producer rents, social entrepreneurship generates additional value through its social benefit. A social entrepreneur aims to maximize impact (rather than profits) to create as much value as possible for the social purpose while ensuring that the business can be sustained through revenues from consumers or other stakeholders. The difference between philanthropy and social enterprise is that a social enterprise is an organization that covers all or most of its costs through a revenue-generating business model, which allows it to pursue the social motive⁷.

However, as argued in the following, societal returns to social entrepreneurship likely go far beyond the immediate welfare effects. Value created by social entrepreneurs spills over to other businesses and individuals via several channels. The first one relates to knowledge spillovers through social innovation. Social entrepreneurs innovate by experimenting with novel ways of product and service provision or through the implementation of new solutions to social problems. Others can learn from these activities by observing successes and failures. Social businesses may, therefore, have a fundamental role in the diffusion of innovative business practices. The second channel goes through the explicit or implicit setting of norms and standards. By leading the way in the innovative implementation of social standards and socially beneficial practices, social entrepreneurs can have an ethical or normative impact on other entrepreneurs. For example, the introduction of new ways of delivering services that address basic human needs, such as the provision of low-cost surgeries to cure blindness or the deployment of sanitation systems in rural villages⁸, constitute social enterprises that implement and develop infrastructure role models that may be taken up elsewhere, including by companies with a for-profit motive. Finally, social entrepreneurship – by focusing on crucial needs that are otherwise not sufficiently addressed – contributes to elevating social issues and thereby adds economic value by either reducing the consequences related to these issues (e.g., crime, health threats, ...) or by restoring the economic performance and contribution of those, directly and indirectly, benefiting from the social enterprise.

Yet social entrepreneurship also comes with significant challenges in the form of the classical hurdles to entrepreneurial ventures, such as financing constraints, the liability of newness, bureaucracy, and regulatory uncertainty. The first and second hurdles stem from the challenge of building a functioning organization from scratch. To raise external financing from banks or investors, young businesses typically need to build a reputation or at least create reliable signals for trustworthiness and quality⁹. Liability of newness, however, affects more than access to financing. It also affects the trust that customers, regulators, other public authorities, beneficiaries, or other stakeholders have vis-à-vis the new social business. Until this is achieved,

young companies often rely to a large extent on the founders' own funds or family and friends. Coping with bureaucracy and regulation is another challenge for most young companies. However, social entrepreneurship with new and unconventional ways of doing business may be particularly challenged by compliance. These factors create a specific set of constraints on social businesses in the early phases of development. Starting a social business while facing many constraints requires particular traits, skills, and motivations¹⁰. Figure 1 summarizes the **Top 5 challenges** – often overlapping and interdependent – for social entrepreneurs.

Figure 1: Top 5 challenges for social entrepreneurs



In addition, the success of social enterprises may be dependent on founders' social and business networks, political connections, and non-conventional funding sources¹¹. Research shows that social entrepreneurs face additional factors that are a threat to the success of social entrepreneurship, including factors such as psychological stress from being confronted with social problems, including violence, critical health situations, or social uncertainty¹². In addition, pressure from certain interest groups can severely impede the work of social entrepreneurs, reducing their incentives and ability to continue the social business. Finally, due to their hybrid nature, balancing revenue seeking, quality, and scope with social contributions comes with strategic and managerial challenges¹³.

These properties of social entrepreneurship, alongside their intrinsic characteristics, stress the need to develop and implement ecosystems and policy designs that account for the direct as well as the indirect effects of social entrepreneurship.

The following chapter is structured as follows. First, we review insights from relevant articles in the area of social entrepreneurship and innovation research. The selection of articles is not intended to be comprehensive and includes selected articles published before April 2024. The literature on social entrepreneurship is large and fast-growing, and the following review is based on chosen bits from this body of research after screening for fit and research quality. The first section of the review focuses on the motivations of social entrepreneurs and innovation driven by social entrepreneurs. The key questions are: What motives drive social entrepreneurs? How do these motivations differ from other entrepreneurs? In this context, we will discuss the private and social returns to entrepreneurial activity.

The second section extends this discussion to the role of social entrepreneurship in competition and innovation by other companies. The key question here is: How do social entrepreneurs affect others' incentives to innovate?

The third section focuses on the economic contribution of social entrepreneurs. The central question is what direct and indirect effects originate from it and who benefits from social entrepreneurial activities. We will distinguish between the first-order and second-order effects of social entrepreneurship on the economy by reviewing insights on the economic performance of social ventures and their spillovers to other agents in the economy.

Section four looks at the broader impacts of innovation in socially-orientated start-ups by theorizing on knowledge spillovers to for-profit businesses or other organizations and through their impacts on norms and standards. Finally, section five concludes and discusses the challenges related to measuring the overall effect of social entrepreneurship on the economy and presents implications for policy support targeted at social entrepreneurs. The main question in this part of the chapter is whether commonly used policy instruments are suitable to foster social entrepreneurship and whether specific demands and barriers of social entrepreneurship require different policy designs.

2. What drives the social entrepreneur? Motivations and incentives for socially-oriented business founders

Social entrepreneurs have long played a fundamental role in many economies¹⁴. Yet, the attention drawn to their work in research and practice gained momentum when 2006 Muhammad Yunus was awarded the Nobel Peace Prize for his effort devoted to and achievements in the area of microfinancing micro businesses in Bangladesh. His activities, which had a sustainable impact on the image of social entrepreneurs, can be seen as one of the main examples of social entrepreneurship, defined as a company devoted to solving a social problem. It seems crucial that this definition stresses the social purpose as the main motivation for starting and sustaining the business. The social business may be founded and owned by an individual, a group of individuals, or investors who reinvest all profits to expand and improve the business. Thus, social entrepreneurship does not imply that the company does not or should not make any profits. On the contrary, it may need profits to build and sustain its activities.

In some ways, social entrepreneurship has some overlap in motivations and purpose with philanthropically motivated individuals¹⁵. The key difference, however, lies in the entrepreneur's commitment to the social enterprise and the degree of innovation inherent to the provision of the goods and services provided by the social business to achieve its social objective¹⁶.

Others have also argued that social entrepreneurship is some form of corporate social responsibility (CSR) defined as the corporate provision of public goods or reduction of negative externalities beyond what is legally required or enforced by regulations¹⁷. The key difference to CSR by businesses more generally is that the main purpose of these businesses is not a social purpose per se¹⁸. Here, we define social entrepreneurs such that the purpose of providing some social benefit is the central motivation of entrepreneurs. Besides these factors, motivation may be similar to that of other entrepreneurs. Personality traits such as altruism, compassion, openness to experience, extraversion, and risk tolerance may matter, especially when starting a business that has some benefit beyond private profits¹⁹.

Mort et al. (2006) stress the role of entrepreneurial orientation and, in particular, innovativeness, proactiveness, and risk-taking as critical traits that social entrepreneurs show. In contrast, Bacq et al. (2016) argue that social entrepreneurs may show traits suggesting a low entrepreneurial orientation.

Chapman and Hottenrott (2024) find baseline personality – as captured by the Big5 personality traits – to predict entrepreneurial orientation. This result underscores the role of founders' character traits, preferences, and personalities in entrepreneurial decision-making. As they show for the case of green start-ups, higher scores for openness to experience and extraversion contribute to the likelihood that founders start companies with environmentally beneficial products, whereas higher scores in neuroticism reduce it. This illustrates that social entrepreneurial activities are also motivated by individual professional satisfaction.

Thus, while personality and preferences appear to be an important factor, the mechanisms through which personality affects social activities are less well understood so far. Hirsh (2010) shows that one channel can be awareness and concern about social or environmental problems, and hence, a stronger perceived need to act or a feeling of responsibility may emerge. In line with this, a comparison between nascent for-profit entrepreneurs and social entrepreneurs by Clark et al. (2018) shows that the latter have higher levels of self-efficacy and are more ambitious.

Thus, the social entrepreneur may be motivated by intrinsic factors such as the above-mentioned personality traits combined with other factors that increase the awareness of a social

issue²⁰. Drawing from the utilitarian theory of behaviour, the social entrepreneur generates personal positive utility from the activity. Therefore, the motives for building a social business may be less dependent on personal financial returns²¹. Although it has long been understood that founders may generate positive utility from risk-taking or from the entrepreneurial adventure, or the challenge as such, the case for the social entrepreneur may depend more fundamentally on the gain from the discovery of an opportunity linked to a social need²².

The social entrepreneurs' reward for effort is, therefore, likely linked to a combination of the social value that the business generates²³ and the founders' own value stemming from (social) preferences and the joy of pursuing a socially beneficial idea. Combined, these factors may contribute to the professional satisfaction of the entrepreneur.

Yet identifying a social challenge often requires exposure to the respective environment in which these challenges occur. Finding solutions also requires familiarity with the environment and the circumstances in which the problems occur. Familiarity with the situation is often a crucial precondition for developing solutions acceptable to the affected population. These might be children, parents, schools, or administrators who are in charge of handling a given situation. Thus, awareness and familiarity allow social entrepreneurs to discover and develop possible solutions that address the involved parties' causes or choices. Bacq and Alt (2018) indeed find that empathy plays an essential role in social entrepreneurial intentions. Still, rather than directly, it does so indirectly through the interaction with agency and communion. Hence, personality traits, preferences, and the environment contribute in complex and interactive ways to whether a person acts upon ideas and opportunities in the form of building a social enterprise despite the challenges that come with it. Figure 2 presents the **Top 5 motivations** for social entrepreneurs, which are typically interdependent and often jointly play a role.

Figure 2: Top 5 motivations for social entrepreneurs



3. The role of social entrepreneurs in competition and innovation

While there are differences between social entrepreneurship and other forms of entrepreneurship, both have in common that founders discovered a segment or area of activity that is worth investing in. The investment involves money, effort, and time commitment, all of which have opportunity costs²⁴. These opportunity costs comprise alternative uses of founders' time and money as well as the foregone income that could have been generated if they did not engage in the social business. As discussed above, the fact that someone decides to build a social business implies that there are intrinsic or sometimes also extrinsic incentives to do so. The decision and subsequent actions, however, affect not only the entrepreneur. By acting in and engaging with its environment, the social entrepreneur impacts products, markets, and the actions of other actors. One impact channel is related to innovation.

Entrepreneurship almost always has some innovative element, as, by definition, creating a new business comes with a certain degree of novelty²⁵. Much of the early-stage entrepreneurial activities of any entrepreneur centre around the knowledge of the needs of a target group, the pursuit of the opportunity, a process of research and development (R&D) which involves

market research, product or service development and design, and evaluation of customer or user feedback. This pursuit of opportunity often implies that by novel combinations of existing solutions, the entrepreneur innovates with the result of new products, services or processes technologies²⁶. Social entrepreneurship can, therefore, be expected to yield innovative solutions – otherwise, it would not be considered entrepreneurial in the Schumpeterian sense. Research in the field of innovation economics has long stressed the impact of innovation on market structure²⁷. This implies that innovative entrepreneurship can disrupt markets and affect the business activities of established organizations.

One central dimension in which newcomers affect the status quo is the pressure to innovate. Innovation by social entrepreneurs or entrepreneurs more generally draws the attention of established organizations²⁸. In some cases, introducing new products or new business practices by newcomers will trigger incentives for existing companies to innovate²⁹. One example is the introduction of new delivery services by established supermarket chains in response to the rise of new, app-based delivery services. In the context of social entrepreneurship, introducing inexpensive medical products, such as the auto-disable syringe invented by Marc Koska for use in underfunded clinics, led to the adoption of similar tools by other hospitals and healthcare providers³⁰. While the idea was later turned into a charity rather than a company, it is the example of an invention brought forward by a socially-motivated entrepreneur with a clear social purpose that created both beneficial effects for the health of millions of people as well as significant economic effects through the reduction in healthcare cost.

This example also illustrates that the newcomer will not necessarily be perceived as a direct competitor by established companies. Social entrepreneurs, with their social-purpose orientation, may not be viewed as competitors. However, their ideas can still serve as an inspiration for other companies, inspiring them to implement or adopt innovative ideas.

Especially in complex areas, such as health care, new ideas and solutions to certain problems can provide organizations with a competitive advantage that is relevant for both social enterprises as well as other businesses. Especially cost-reducing or quality-enhancing innovations or the implementation of novel ways to deliver a product or service to reach hard-to-get customer groups may be copied by businesses with a non-primary social motive. The development of more comfortable healthcare apparel by the manufacturer FIGS, for example, whose main idea was to donate scrubs to healthcare professionals in resource-poor countries with the aim to increase job safety, soon resulted in the diffusion of the design also among healthcare clothes manufacturers more generally thereby disrupting the market for professional clothing for health professionals³¹.

This process can be described as absorbing knowledge spillovers from entrepreneurial activities³², whereby the learning can be both from failure and bad experiences as well as from success³³. In some cases, learning from outside the organization can be a particularly attractive approach to foster innovation, that is, when internal path dependency is high and processes are sticky³⁴. The extent to which the new knowledge is of value to other organizations depends on several factors: The degree of newness, the extent to which the knowledge is protected by intellectual property rights, the transferability of the knowledge to other applications, and the value that markets attach to products and services related to it. These factors are not straightforward to assess. Experienced entrepreneurs and managers, however, are likely capable of judging the relatedness of a social enterprise's innovation to their own. In the context of social entrepreneurs, the learning from innovation can be of a technological nature in the sense of processes, products or service provision. It may, however, also be related to organizational design, marketing innovations, customer and public relations, or supply chain management. For example, OneWorld Health, a US-based not-for-profit pharmaceutical firm, developed novel ways of stakeholder engagement and implemented a re-designed value chain to deliver effective drugs to developing countries³⁵. The innovation spillover may not only happen within the business sector. Some examples of social businesses initiated government actions to address the problem at a larger scale and with more significant resources. Unis-Cité was a social enterprise founded in 1995 in France with the objective of bringing together young people with diverse backgrounds to pursue volunteer work in social projects³⁶. The initiative was later financially backed by the government and extended to include other non-profit actors who pursued similar programs³⁷.

Thus, the uptake of an activity by a social entrepreneur implies some form of innovation that can benefit the economy more widely and beyond the social purpose through knowledge spillovers and learning.

4. First-order and second-order effects: The economic contribution of social entrepreneurship

While the main goal of a social enterprise is to resolve situations of personal or social deficiency through a business, the benefits may go beyond the initially intended social purpose. Despite the potential relevance of social impact as the most direct outcome of social entrepreneurship, standards for measuring an organization's social impact are underdeveloped on both theoretical and empirical grounds. Research on impact measurement of social entrepreneurship stresses that the phenomena of generating economic value and social value, i.e. dual value creation, is the ultimate output of social entrepreneurship distinguishing it from philatropy, charity and social government programmes³⁸.

More fundamentally, it seems necessary to differentiate between an organizational and a societal perspective when assessing the total returns to social entrepreneurship. In addition, immediate and follow-on effects are both of critical relevance. The former effects play a role in any static analysis of social value social entrepreneurs create. However, taking a more dynamic view of the impact of social entrepreneurship draws attention to the potentially even larger follow-on effects³⁹. Several examples illustrate this. For instance, Medic Mobile was founded by Josh Nesbit in 2009 with the goal of providing mobile and web tools for health workers, hospitals, and patients. By training and equipping several thousand health workers with mobile technology, including free communication and analytical apps, Medic Mobile has improved various *health care and health outcomes*, for instance, by substantially reducing maternal and neonatal mortality and treating malnutrition in children and young adults. Besides these direct socially beneficial effects, the business has triggered follow-on effects through the diffusion of knowledge through training and the development of similar applications by other companies. In line with this example are initiatives that improve *water, food, and housing access*.

As argued above, innovations first implemented by social entrepreneurs often get replicated in other settings or geographic regions⁴⁰. The emergence and growth of the microfinance industry is another example⁴¹. Initiated by social entrepreneurs, the diffusion of innovative tools for improving *access to financing* has contributed to *boosting economic development* in several parts of the world. For the economy as a whole, this implies that social entrepreneurship can be the source of new business models and the creator of entire industries, thereby re-directing resources to neglected societal problems at large⁴². Another essential impact area is *environmental protection*. Social entrepreneurs can have an essential impact on implementing business practices and consumer behavior, thereby shaping the awareness of pollution and wasted resources. By experimenting with novel approaches, social businesses can affect and shape environmental practices beyond the individual case by setting standards and norms.

By doing so, the social entrepreneur generates second-order effects that are likewise socially beneficial. Again, as in the case of the first-order effects, the entrepreneur is not directly compensated for these benefits created through the initial social business activity. Some of the wider effects of social entrepreneurship can materialize through 'standard setting'. One example of standard setting in the social entrepreneurship case is building on the 'entrepreneurship as emancipation' perspective⁴³. Encouraging entrepreneurship among women has been shown to have beneficial effects beyond the economic situation of women entrepreneurs. The benefits extend to their families and communities. It facilitates escaping ideological constraints and constructing new meaning in life and new social roles and connections that provide a platform for building a stable income and social environment, not only in the context of developing countries. By permitting financial and social autonomy, it *empowers women* while, at the same time, the business often addresses previously neglected aspects that are more relevant to women or children. Again, the contribution of social entrepreneurial activities that aim to foster entrepreneurship by women through access to finance or other crucial resources generates the main social and economic impact via second-order effects that widely shape standards and norms⁴⁴. Similar examples exist for entrepreneurial efforts to improve *work safety and labour rights* or access to *education and training* – especially for young people – where the effects go far beyond the individuals who initially benefited from the social business. Better educated and

trained individuals may be more likely to generate economic and social value themselves. Other initiatives have led to improved living and work situations for *minorities* with beneficial effects beyond the targeted groups.

Through these various channels, social entrepreneurship has also been shown to be influential in the fight against poverty⁴⁵ and in developing strategies for inclusive growth in subsistence marketplaces⁴⁶. Moreover, it has been a contributor to social transformation and even institutional change with positive effects on *civic participation and culture*⁴⁷. It is, therefore, important to stress that the effects of social entrepreneurship often go beyond the initial area of activity. Positive impacts of access to education and professional training, for example, can benefit the economy and society more broadly than just raising the income and well-being of the initial beneficiary. Such positive spillovers can be seen in virtually all areas of social entrepreneurship and should be considered when evaluating the overall impact of social businesses. The **Top 10 impact areas of social entrepreneurship** – taking into account first and second-order effects – are summarized in Figure 3.

Figure 3: Top 10 impact areas of social entrepreneurship



5. Conclusions and implications for a policy framework for social entrepreneurship

Researchers, policymakers, and the general public are increasingly interested in understanding organizations that address both economic and social needs. Social enterprises have gained attention in recent years as hybrid organizations combining social purpose with market-based approaches to funding and sustaining their activities⁴⁸. It is, however, a challenge on its own to measure the **total impact (Figure 4)**, i.e., the societal and economic impact of such activities⁴⁹.

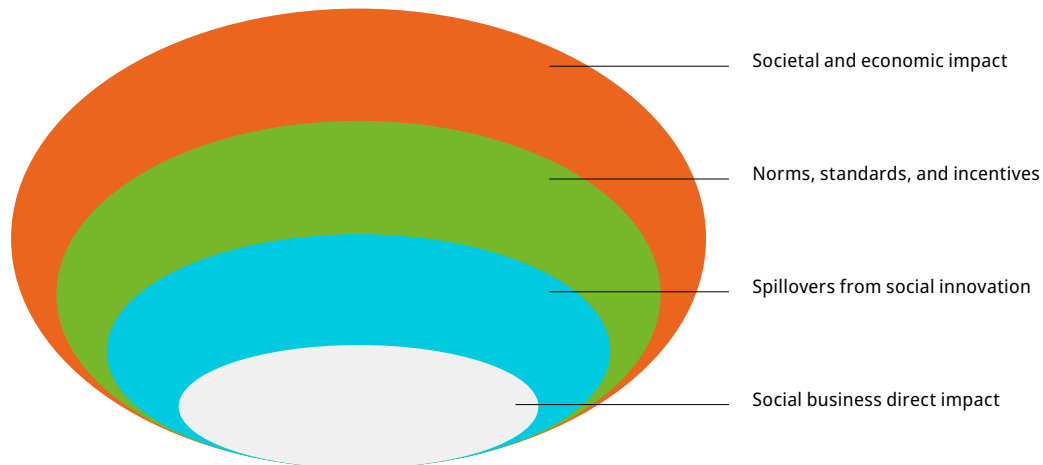
Measuring the performance of social businesses is inherently difficult due to their hybrid nature and the social complexity associated with their activities⁵⁰.

This article argued that measuring the direct impact of social businesses may even fall short of its true impact. Focussing on the social purpose as the first-order impact means that significant second-order effects of such activities are not adequately accounted for. These second-order effects have multiple dimensions – all of which may be highly important when assessing the overall impact of social entrepreneurial activities. In particular, spillovers from social innovation either directly – in the form of knowledge transfer and learning – or indirectly through creating incentives to innovate for other organizations can multiply the impact of social entrepreneurs

beyond their own beneficial impact. Two such examples are the social IT business Medic Mobile and its impact on digitization in health care provision or the medical clothing company FIGS.

Moreover, the social impact can multiply through *standards and norms* set by social entrepreneurial activity and are subsequently adopted by other organizations that we would not classify as social enterprises as they pursue mainly non-social objectives. Others may adopt certain practices and redirect some of their returns to further social purposes or implement practices that generate social value within or across organizations.

Figure 4: Total impact of social entrepreneurship



It seems, therefore, crucial to account for both social returns that are directly generated by the social entrepreneur and those social returns that are generated via the diffusion of innovation and the adoption of social practices by others.

The complexity of assessing social entrepreneurs' overall economic and societal impact becomes apparent when considering the economic returns companies generate from social entrepreneurship and the economic impact that stems from reducing social friction. Social innovation in health care, for instance, generates a direct impact on health and, hence, likely a positive economic impact at the individual level as well as a broader economic impact from the reduced negative implications of disease on the economic contribution of an individual. Other examples can be found in social entrepreneurship, which focuses on providing education or labor market integration for disadvantaged subpopulations. Taking the example of micro-financing businesses and thereby providing an opportunity to generate income by individuals who do not have access to loans by any other means is another case that illustrates the broader impact of social entrepreneurship that may even span generations⁵¹. It shows that the loan receivers and their customers, suppliers, and families benefit. Higher and stable incomes may imply more room for investment in education, nutrition, and health care, which has beneficial follow-on effects far beyond the initial provision of affordable loans. In this case, the private profits made by the loan receivers can be considered part of the social impact. Here, the social and economic impact goes beyond the effects of the individual beneficiary by reducing negative side-effects of exclusion from education or work. Many social entrepreneurial activities thus benefit other entrepreneurs, consumers, and communities. To illustrate this, social enterprises have been shown to create employment and, hence, a source of income in areas that would otherwise not have grown⁵². CIRIEC (2012), for instance, show that the number of jobs created by social businesses corresponded to 6.5% of the total workforce in the EU-27. Notably, the employment stays in local communities, so the major contribution of these businesses multiplies at the local level. Given that such businesses are typically located close to the place of need, they play a fundamental role in social inclusion and enhancing local social capital.

These examples illustrate that the impact assessment of social entrepreneurship is not only complex because of the difficulty of quantifying the direct social benefits. It is also extremely challenging to grasp the more comprehensive, often indirect impacts. Evaluating the returns

to social entrepreneurship based on the performance of the individual business will likely fall short of the actual impact. Even failed businesses – in the sense that the entrepreneurs could not maintain the activities – may have already generated second-order impacts, some of which made the initiative perhaps obsolete.

The key issue is that neither the social entrepreneur nor the investors in social businesses are compensated for the broader social and economic returns they create. From a welfare perspective, this implies that some of the benefits generated by social entrepreneurs are distributed to the owners of other enterprises, who do not necessarily spend additional returns on social investments. In some cases, adopting some practices by other actors may render the activities of a social business obsolete. Several examples of social initiatives have later been institutionalized, such that either the government (for example, bringing young people into employment) or other companies (producing cheaper medical equipment) have taken up the idea. These indirect returns matter for the overall returns to social entrepreneurship as they shape the incentives for engaging in social entrepreneurship. Yet the previous discussion of the motivations of social entrepreneurs suggests that – unlike other forms of entrepreneurship – they are rather non-monetary and shaped by the personality traits and preferences of the founders. In many cases, exposure to specific problems creates awareness and the need to find solutions. Thus, monetary rewards or the threat that the business model may become obsolete are not at the center of social entrepreneurial activity. The latter point may even be a central goal for social entrepreneurs.

Research, however, also shows that institutions matter for the success of social enterprises and that social entrepreneurship cannot compensate for institutional failures⁵³.

Governments and other institutions are needed to design, supervise, and enforce the legal framework in which social businesses operate. Unfortunately, in many cases, the need to address social problems is highest in places where institutions are weakest. This institutional infrastructure includes property rights – including intellectual property – and the rule of law, as well as effective competition policy. The better functioning these institutions are, the more likely it is that social entrepreneurial activities can generate direct and indirect effects.

If established organizations abuse their power or develop strategies to increase entry hurdles for social entrepreneurs, these practices harm the entrepreneur and the social objective⁵⁴.

Some social businesses address goods that can be labeled as public goods in the sense that they are both non-rival and non-excludable. Non-rivalry implies that one individual's consumption of the good does not preclude others from consuming it. Non-excludability means that there are no mechanisms to prevent individuals from consuming the good once provided. Examples include education, clean water or clear air, and certain types of digital and physical infrastructure.

Since public goods tend to be underprovided in most markets and, in particular, in countries with weaker institutions, there is a substantial need for social initiatives. While some of the need is addressed by governmental and non-governmental organizations or charities, social entrepreneurs have invented innovative approaches to the provision of public goods in places where other organizations initially failed to step in or became only active later following up on the practices of a social enterprise. In some cases, we see the transformation of public services into social enterprises. Greenwich Leisure Limited in the United Kingdom is one example that illustrates 'social franchising' as another form of replication of social entrepreneurship. Social franchising is often managed and coordinated via platforms such as the European Social Franchising Network and provides one route to the broader institutionalization and diffusion of social initiatives⁵⁵.

A central challenge for social entrepreneurship is access to financial resources. While this is a common hurdle among young companies, it is even more pronounced in social entrepreneurship, where founders rely to a large extent on their own funds, crowdfunding, or creative fundraising for collecting seed financing. While the entrepreneurs themselves may not be profit-driven, they still need to be able to purchase necessary equipment and pay for staff and support. Thus, individual and institutional investments are likely to play a key role. Solidary financing and venture philanthropy are two sources of financing that are quite specific to social businesses. Still, the extent to which founders rely on different sources of financing is largely

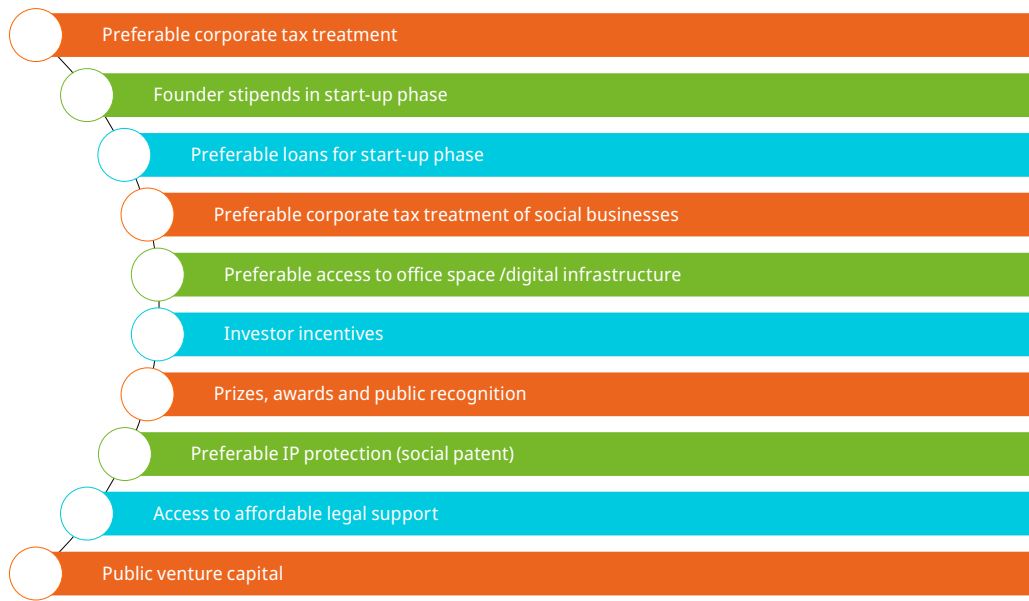
unknown. Ethical or social capital markets are growing, but their relative liquidity is presumably rather low, and some of such markets have also failed in the past⁵⁶.

These factors make a strong case for policy support for social entrepreneurship. Social enterprises play an essential role in addressing social and environmental challenges, fostering inclusive growth, and contributing to social inclusion through their activities. Besides the direct effects related to the main social objective, there are further effects through innovation and spillovers that generate additional societal and economic returns. For example, numbers for start-ups in Germany show that environmental goals are increasingly important, with more than a third of new businesses declaring to offer products or services that benefit the environment⁵⁷.

In many cases, the initially required investment volume to achieve this is rather small compared to expected social benefits. Supporting social entrepreneurs' efforts such that the business (not the private entrepreneur per se) is compensated for the social benefits it may create seems, therefore, plausible. Public social entrepreneurship funds could be one policy tool that could reduce hurdles for socially motivated businesses. Some countries have also introduced special legal forms for social businesses in a variety of designs. These legal forms come with special treatments for companies with a social purpose. The legal form benefits from specific tax rules and even the exception from corporate taxes if profits are re-invested into the business. However, in many countries, social entrepreneurs still use and adapt legal forms without specific benefits⁵⁸.

When supported through public policy, the social entrepreneurial endeavor may also be more successful – hence avoiding the cost of failure and increasing the social returns in case of success. The overall returns to social entrepreneurship may be higher than the initial investment in financial or infrastructural support or foregone tax income. However, all entrepreneurial activity comes with substantial risk and the possibility of failure. This is also the case for social entrepreneurship. There may also be high opportunity costs of investing public funding in social business and not into entrepreneurship more generally. It seems, therefore, plausible to treat social entrepreneurship similarly to high-tech entrepreneurship, where society faces a similar risk-return ratio and much of the *government support* is justified based on second-order effects related to entrepreneurial activities⁵⁹.

However, evaluating the rate of return to public spending on social entrepreneurship is not trivial. The returns to government investment into these businesses also include indirect effects such as reduced payments on social benefits programmes, lower spending on crime prevention and prosecution, and additional income from income taxes and social security contributions if the social business created employment directly or indirectly through social inclusion. Additionally, it should be noted that – unlike in the case of charity – there is a business model behind the social enterprise that ideally should generate income such that the social firm can sustain itself through the direct cash flow from the business that it engages in. Policy measures to support social businesses may, therefore, be especially important in the early phases of the life of a socially motivated company. Targeted tools and policy instruments may help founders to overcome the initial hurdles and constraints. A mix of measures from the Top 10 policy tools (Figure 5) is likely most effective in addressing the needs of diverse areas of social entrepreneurship and thereby allowing the unlocking of the full societal and economic returns of social entrepreneurship.

Figure 5: Top 10 policy tools to foster social entrepreneurship**Notes:**

- 1 Short *et al.*, 2009, Battilana and Dorado, 2010; Dacin *et al.*, 2011, Saebi *et al.* 2019.
- 2 Austin *et al.*, 2006; Stevens *et al.*, 2015; Gertner, 2023.
- 3 Stephan *et al.*, 2016; Doh *et al.*, 2019.
- 4 Santos, 2012, Rangan *et al.*, 2006.
- 5 Dees, 1998; Martin and Osberg, 2007.
- 6 Santos, 2012; Markman *et al.*, 2019.
- 7 Tracey *et al.*, 2011; Gertner, 2023.
- 8 Seelos and Mair, 2005.
- 9 Lins *et al.*, 2015; Berger and Hottenrott, 2021.
- 10 Lumpkin *et al.* 2013.
- 11 Sorenson *et al.*, 2006; Noya and Clerence, 2013.
- 12 Tobias *et al.* 2013.
- 13 Nega and Schneider, 2014; Gertner, 2023.
- 14 Urbano *et al.*, 2017, Saebi *et al.* 2019.
- 15 Acs *et al.* 2013.
- 16 Dacin *et al.*, 2010; Lumkin *et al.*, 2011.
- 17 Kitzmueller and Shimshack, 2012.
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