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**Scaling for Significance:**

**Schumpeter Meets the Social Sector**

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*The Enduring Tradition of Social Innovation, Social Change, and Social Entrepreneurship*

1. Social entrepreneurship -- understood broadly as efforts taken by individuals to improve the quality of individual and collective life – have been important part of human history and progress since at least the beginning of recorded history. Indeed, from one point of view, both our history and our current condition is the cumulative result of social initiatives launched by individuals from different positions in society, focused on achieving different purposes, mobilizing material assets and human energy through varied means, and deploying those assets through different operational activity to achieve the desired results. As Margaret Mead has famously observed, “Never doubt that the world can be changed by small groups of individuals. It is the only thing that has ever done so.”
2. In recent decades, however, the concept of *social entrepreneurship* has emerged as a distinctive practice in the much wider field of social innovation and social change-making. The practice is seen as distinct from familiar forms of *commercial entrepreneurship* in that the individual entrepreneurs (and the enterprises they create) are motivated and guided to achieve social purposes that commercial markets (as they are currently operating) do not seem to reach – leaving particular individuals more miserable and more oppressed than individuals living in a good or just society could happily accept. The practice is seen as distinct from the familiar form of *social and political reform movements* in that it seeks to use market mechanisms to deliver not only economic welfare to those at the margins of existing market economies, but also to help those at the margins of society to find dignity, solidarity, safety and voice in the societies in which they live – largely, but perhaps not exclusively through enhanced economic activity and success.
3. The concept emerged as a distinctive practice in large part because it attracted the kind of social attention that takes a familiar, widely present (if not much remarked) social phenomenon and turns it into “the next new thing” – something that we think we have not seen before that seems to promise great things for the future. Articles and books about social entrepreneurs were written that presented compelling stories of individuals who had made significant economic, social, and even political changes in society from little more than an invincible commitment to a righteous cause, and an ability to spot and exploit opportunities for making social progress that others had missed. The heroes in these stories became celebrities as honors, rewards and prizes were bestowed on them for their accomplishments. To stimulate more individuals to pursue this form of social change, new prizes and competitions were created to create thousands of new social entrepreneurs for any single “winner.” Academics drawn to the “next new thing” began studying the particular cases and on that basis, offer commentary on questions ranging from practical questions focusing on the distinctive practices of social entrepreneurs that seemed to distinguish those that were successful from those that were not, and the degree to which the emergent practices had the potential to transform conditions in domains that had not yet been invaded by this new form of social change.
4. The shift from a *phenomenon* driven by the simple desires of particular individuals to ameliorate (or ideally solve) important social problems in ways that had eluded existing commercial enterprises, nonprofit organizations, and government agencies to a self-conscious, well financed *movemen*t was aided by a powerful resonance between these ideas, and the lived experience of a new kind of philanthropist that had emerged in society. Tech entrepreneurs had generated considerable wealth, along with transformative social change precisely through the creation of innovative ideas that could be spread widely through market forces (once the innovations could be attached to a “business model” that could generate revenue streams from the new information technologies they had created). They knew, based on their own experience, that imagination and innovation could transform commercial markets and economies. Why wouldn’t a similar process, indeed, even one that rested heavily on the new information technologies, be able to transform the social conditions that commercial markets had not yet reached?
5. The idea that social progress could be made through the methods of entrepreneurship operating in consumer driven competitive markets also found its appeal in conservative political ideologies whose enthusiasts sought to shrink the overall importance of government in society, and to make what remained of government much more efficient and effective in achieving the social goals that remained for government to solve. Surely, both technology in particular, and entrepreneurship that sought to develop and spread new practices and methods could challenge and improve the practices of existing producers in the voluntary sector and government that sought to improve social as well as economic conditions.
6. From these influential perspectives, the important enemies were the existing social institutions in the voluntary sector and government that had sopped up much of the money that society had made available for advancing social purposes not achieved by markets, and continued to waste that money on ineffective activities. What was needed to deal with stubborn social problems, and respond effectively to challenging emergent problems was not the stagnant bureaucracies of government or even the long established nonprofit organizations, but the dynamic influence of the new breed of social entrepreneurs.

*The Social Entrepreneurial Movement*

1. In fairly short order, then, a movement – complete with celebrated practitioners, a more or less well developed set of practices, a track record of accomplishments, streams of financial support, and an ideology that could both explain why the movement was important at this particular moment, and how it could on to even greater accomplishments – seemed to overtake the wider field of social innovation and social change. This transformation from unremarked social phenomenon to celebrated social movement may well have encouraged many individuals who did not think of themselves as potentially important social change agents to re-consider, and in doing so, may have swelled the ranks (and changed the practices) of social change makers around the world. But it is also possible that many of those who were suddenly viewed as part of this grand movement were the social change-makers that had always been present in the society – the individuals who dreamed of a better world, had an idea about how to do it, and took up positions and developed careers that allowed them to pursue their dream.
2. While there can be debated about exactly when the social entrepreneurial movement began, it seems that we have been thinking about, encouraging, observing, and evaluating efforts within the movement for at least a decade, perhaps two. That period has seen some significant successes, and the development of new ideas that seek to generalize from these successes to a wider set of possibilities than the particular enterprises that formed the basis for the theory. These concepts include such ideas as the following:
   1. “bottom of the pyramid” opportunities for both commercial growth and the alleviation of social problems:
   2. “corporate social responsibility movements” that have brought social and political pressure on private corporations to go beyond their legal requirements to improve individual and social welfare by refraining from acting in ways that harm social welfare, and engaging more actively in ways that improve social welfare
   3. “hybrid organizations” designed and managed explicitly to produce a mix of financial and social returns as a form of blended value;
   4. “social enterprises” that have developed more efficient and effective methods for achieving particular social results in domains such as health care, education, and child care and depend on “earned revenue” from beneficiaries as well as third party payers such as voluntary contributors and government financial support

While these concepts differ from one another in important ways, they are similar in that all seek to identify and exploit explicit ways in which primarily (but not exclusively) market enterprises (private enterprises focused on earned revenues from consumers of products and services) and market forces (consumer demand for goods and services spread across firms in competitive markets) might be engaged in the solution of social problems; thereby ending the long stagnation of productive capacity in what could be described as the social or public sector.

Conspicuously missing from the list above are the kinds of social change efforts that focused their attention on changing social values, political engagement, and public policies through civil society and policy advocacy organizations. Such movements continued to exist in the world as important social change efforts, led by individuals and voluntary associations that had been called into existence by indignation about one social condition or another. And, they were often included in the broad umbrella of social change efforts.

But, because these movements seemed to focus on social relationships, and particularly on enhancing the status of those who had been socially and politically as well as economically marginalized and oppressed; and because they seemed to operate outside the commercial sector, in the different domain of civil society and politics; and because they often depended more on political means and public policies to achieve their social goals rather than markets, they were not seen as central to the new movement. In fact, one could reasonably say that it was precisely these forms of social change that the new movement for social entrepreneurship rejected. In this piece, I aim to show that this explicit rejection of social and political movements, and the potentially important role of government in enabling or defeating the potential of the social entrepreneurs may have been an early, critical mistake that has limited both the actual and potential accomplishments of the social entrepreneurial movement.

*Facing Up to the Uncertain Results*

1. Despite the many particular successes of “social entrepreneurs” acting in alignment with one or more of the ideas described above, it is not at all clear that these efforts have “moved the needle” much in producing an impact on important social conditions. If we used the framework of the International Declaration of Human Rights as a device for identifying the particular social conditions that could be viewed as the special target of producing enterprises in the social or public sector, and we reviewed the principal indicators of impact, it would be hard to say that the social entrepreneurial impact has had much impact. Even the greatest success of social entrepreneurship – the micro-finance industry – has had only limited results when measured against the scope of the problem whether observed at the output level (access of the poor to reasonably priced credit) or at outcome levels (number of individuals moved out of poverty by virtue of improved access.)
2. Whether one looks at performance across these sectors from the macro perspective, or consults the social entrepreneurs who have been laboring in the vineyards for years to produce precisely these social and public results, the problem looks the same: the innovative ideas about how to solve social problems using private enterprises (both commercial and voluntary) organized in markets where firms compete to achieve the desired results does not seem to be working. The enterprising initiatives seem to get stalled at the point after the ideas have been developed, after they have been fielded and tested, and just at the point where the entrepreneurs are looking to tap into a large stream of revenues (evidence of public support) that will carry their initiative to scale and impact.

*Re-Thinking the Theory and Practice of Social Entrepreneurship*

1. This raises tough questions both for those who have chosen to become social entrepreneurs, and for those who have been supporting and commentating on the emergence, accomplishments, and potential of the movement. Why are the initiatives that seem so promising stalling? Why is it that the cumulative effect of social entrepreneurial efforts do not seem to be producing impact at scale? What is wrong with the theory of social entrepreneurship that claims a significant capacity to make transformative social change in key social sectors? What is wrong with our practices?
2. I have a simple answer to these questions: those of us who have yammering on about social entrepreneurship have allowed ourselves to be misled by a compelling theory about what drives dynamic efficiency and productivity in commercial markets, and assumed that the process would be roughly similar in the social sector. The big mistakes lie first, in failing to understand the nature of the *demand* that animates and guides productive activity in the social sector, and second, in failing to understand exactly how the *demand* for social changes interacts with those who would like to supply social change by creating the organizations that can produce social impact at scale. To understand what we need to do next, we will have to shed the simple general theory and ideology that has so far guided and supported the social entrepreneurial movement, and learn how to analyze the empirical facts that describing the structure, conduct, and performance of particular social industries, and particularly the forces that are encouraging or impeding sustained productivity gains in those industries. Let met develop these ideas in a bit greater length.

*The Gospel According to Schumpeter: Entrepreneurs as the Key to Dynamic Efficiency*

1. To no small degree, it is the thinking of Joseph Schumpeter that fires the imagination of those who are most enthusiastic about the social entrepreneurial movement. It was Schumpeter who drove economic theory beyond its concerns for *allocative efficiency* (ensuring that producing firms made products and services which individuals really valued and would pay for), and for *technical efficiency* (creating competitive markets that would force producing firms to find low cost methods of producing particular goods and service not only to maximize profits but simply to survive), and added an important focus on ***dynamic efficiency*** (the challenge of ensuring sustained productivity gains in the economy as a whole as new technologies and new demands emerged.) He emphasized dynamic efficiency because it was dynamic efficiency that would produce increased social welfare over the long run. And the key to dynamic efficiency, Schumpeter argued, was a large supply of profit motivated entrepreneurs prepared to run the risks of challenging the status quo by introducing new production processes, new products, and new services into existing markets dominated by older, less efficient processes and less desirable products and services. This constant supply pressure from entrepreneurs, combined with consumer demand that animated and guided the productive activities of the economy as a whole, would create a “gale of creative destruction” that would force low performing firms out of business, freeing up both capital and consumer dollars to fuel the growth of new and better production methods, and new and better products and services. Productivity would increase.
2. This compelling image of the conditions that encourage dynamic efficiency in the commercial sector has cast its spell over our thinking about how to improve productivity in the social sector as a whole. If only there were enough entrepreneurs with good ideas! If only they could have the funding to develop and test their ideas! If only they could gain entry into existing markets! If only the existing markets could reliably recognize the value of the new ideas! If only investment dollars and revenue streams would flow to the valuable new ideas, then, social entrepreneurs could create a “gale of creative destruction” in those social sector industries that were struggling with both the stubborn, chronic problems that have long been with us (poverty, malnutrition, ethnic hostility, social oppression), and those that are newly emergent (global warming, huge increases in international migration that stretch both the economic capacity and social tolerance of the communities to which immigrants come, the global spread of disease and the emergence of drug resistant bacteria, etc.).
3. That compelling vision focused our primary attention on the “supply” side of the social sector – the array of organizations that mobilized and deployed assets to produce material changes in the quality of individual and collective life; and more particularly, on the innovative entrepreneurs who were prepared to challenge dominant ideas about how best to deploy assets to achieve the desired social results. In this vision, the enemies of progress in social sector industries and enterprises were: 1) established nonprofit service organizations which were scattered, small, tied to tradition, and insufficiently accountable for producing real social impact with the funds they held; and 2) the government which had been captured by its own agencies and become the protector of “producer monopolies” in both the nonprofit sector and government instead of a collective consumer focused intently on achieving allocative, technical, and dynamic efficiency among the producing enterprises in varied social sector activities.
4. Much less attention was given to the “demand” side of the social sector – the flow of revenue that would enable the new ideas not to launch, to sustain themselves over time, and to reach a scale that could produce a significant impact on social problems compared with what societies had been able to achieve before.[[1]](#footnote-1)
5. Unfortunately, what we have learned is that problem may not have been on the *supply* side of the social sector, but instead on the *demand* side. There were plenty of individuals with ideas and a willingness to pursue them with limited hopes for individual financial success. The important question was exactly who would pay the various prices that had to be paid to develop, test, and (most importantly and most expensively) *scale* the ideas to achieve significant social impact. And it is on the demand side that some of the most important differences between the commercial sector (which was Schumpeter’s focus) and the social sector (which is the focus of those interested in social entrepreneurship as a key drive of social change) appear and become most troubling.

*The Demand Side in Schumpeter’s Theory of Commercial Dynamic Efficiency*

1. To begin, it is useful to review the important roles that the demand side of the market plays in Schumpeter’s theory.
2. First, the existence of a large existing and latent financial demand for some specific product or service is an essential precursor for any commercial entrepreneurial activity. An entrepreneur can start out with a wholly new product for which no demand currently exists, and hope that the appearance of the product will uncover and exploit the previously hidden demand. Or, an entrepreneur can identify and seek to exploit a particular niche in an existing market that he or she can serve better than current suppliers. Or, an entrepreneur can make an assault on a large well established market, and seek a dominant market share in the industry on the strength of the quality and price of his or her product or service. On occasion, entrepreneurs can create whole new industries that did not previously exist. But which of these outcomes is possible depends critically on the potential, aggregate financial demand for the good or service. All productive activities take money to sustain themselves and grow. And, since the important source of revenues in the Schumpeter model is consumer demand, the latent demand for social change is limited to what individuals will buy for themselves.
3. Second, it is the promise of the financial returns to be earned by sales to enthusiastic customers that provides the principal motivation for Schumpeter’s entrepreneurs, and those risk taking financiers who are prepared to share the risk of developing the ideas with the entrepreneurs in exchange for a portion of the financial returns once the innovation succeeds. That is the role of the profit motive in the theory, and it works not only to motivate the entrepreneur to spend his own “sweat equity”, but also others with capital to invest who believe in the innovator’s idea.
4. Third, to be financially successful, the innovative process, product, or service has to be more or less precisely fitted to the desires of the customers who make the market for a particular class of goods and services, and work to meet their demands. This is the place where imagination has to be disciplined by specific, concrete knowledge of what consumers want or think they need, and the product or service engineered to meet those specific wants or needs. The technical skills of marketing analysis, product or service design, and production engineering have to be deployed to give a good idea about a new product or service a chance to succeed.
5. Fourth, the critical choices to switch from an old product or service to a new version that can replace the old, and in doing so naturally add resources to the new product and take them away from the old, are made at by individuals on a highly decentralized basis. Consequently, a good that is only a bit better, or appeals to only a small market will have a chance to survive and improve. But a good that is a lot better and appeals to many individuals will be able to scale rapidly. This creates both room for and an avenue for growth and replacement of the less good old (judgement by a heterogeneous market) by the better new.
6. Fifth, from a social point of view, consumer choices to buy new products or services are taken as an objective evaluation of the worth of the new product or innovation. If a new product earns more revenues than it costs to produce, and grows from a niche to dominate an entire market, society assumes that the new thing is something worth producing, and better than other products. No further evaluation or testing is usually required. The consumer with money to spend is the undisputed arbiter of the value of the new produce and service.
7. Sixth, again from a social point of view, the overall level and distribution of a new good or service that is produced by entrepreneurs and consumed by customers is assumed to be the right level since supply and demand are in equilibrium. If the demand were greater, the supply would be forthcoming. If the demand were less, the supply would appropriately decline.
8. In sum, the “demand side” of consumer markets plays a critical role in: a) creating a persistent, all- encompassing demand for improved products and services; b) a motivation to entrepreneurs (and venture capitalists) to meet that demand; c) a set of technical requirements that have to be met by any new idea competing for attention; d) a process that allows new ideas to be developed and find their place in a particular industry; e) a reliable method for distinguishing a good idea from a bad one once it appears; and f) assurances that the appropriate amount of a new good or service will be supplied once supply and demand are in equilibrium. ) It is the powerful directional force of consumer demand, acting simultaneously as the arbiter of value, and the provider of revenues to sustain and grow the new enterprise that turns the turmoil of “creative destruction” into the assurance of sustained productivity gains.
9. This is a familiar enough analysis. But one important conclusion one could draw from this analysis is that the reason that entrepreneurship is so important to dynamic efficiency in commercial markets is that is *the entrepreneurs who explore the risky space between what is currently being produced and sold (the status quo), and what could be produced and sold that would be better than what currently exists (the production possibility frontier).* This search is inevitably a bet. And it is a bet made by an individual who is thinking both about the demands that could be met if only there were a good product and service on one hand, and what it would take to field a product or service that could meet that old or new demand on the other. In this respect, the entrepreneur has *to operate on both sides of the market* – as an expert in what might be valuable to produce because it meets demands, and an expert in seeing how that valuable product or service could be produced. It is in those calculations that the crucial “delta” for changing the existing status quo is made. One could say that it is those who can see how to fill a gap between what is valued and what can be produced that are the drivers of improved economic performance.
10. The key question for us is how does this understanding of the role of the demand side in animating and directing entrepreneurial effort to dynamic efficiency in commercial markets help us to understand and help create the conditions under which the demand for improved social results could enhance the dynamic efficiency of the social sector?

*Looking Closely at the Demand (Support) for Social Change Efforts*

1. In commercial markets (as described in economic theory) consumer demand plays two critical roles in giving rise to and shaping productive activities on the supply side of a market. The first is simply the important practical fact that the willingness (and capacity!) or large numbers of consumers to plunk their hard earned money down to buy a particular product or service supplies the wherewithal to sustain a productive activity at a given scale. If consumer demand for a given product or service tails off, the work on the supply side will tail off as well. It is the revenue stream from customers that sustains and scales the commercial firm.
2. The second important role is that consumers are viewed both by themselves, and by the wider society as the appropriate arbiters of the social value of what they are purchasing, and the value of the productive activities and use of resources necessary to produce their particular goods and services. It is assumed that if individuals voluntarily buy a good or service, that the good or service is valuable to them, and since it is consumers who are sovereign in the market, their judgment as to value aligns with society’s judgment as to value. It often follows from this key assumption that the overall, aggregate level and distribution of the production of particular goods and services that can be supported by consumer demand is the appropriate level and distribution to supply. That is what it means for the production and distribution of a particular good or service to be “in equilibrium:” the supply equals the demand (when the demand is understood to be the sum of those willing and able to pay for the consumption or use of a particular good or service.)
3. A key characteristic of the social sector within which and for which social entrepreneurs typically do their work is that the basic structure of the demand side departs from this “consumer” model of demand. It departs from the important practical question of where the money will come from to support the development and (most importantly) the *scaling* of innovative social change enterprises that are more effective than current suppliers. And less obviously but equally importantly, it departs from the important question of which actors in society become the important arbiters of the social value that is being produced by individual social change firms on one hand, and by the collection of social change firms in given sectors on the other.
4. It is important to see that consumer demand does not disappear from the scene. Indeed, if one wants to stay close to the market analogy from which Schumpeter’s theory is derived, it is natural to start with the demand for social entrepreneurship that comes from individual consumers with money to spend on improving their own conditions. Indeed, a liberal society is built on the idea that individuals have both the right to be free (to live autonomously and with dignity), and the obligation to avoid becoming a problem for others. Those rights and responsibilities create a space within which individuals seek to engage in activities that could protect them from material ills such as poverty, physical disability or sickness, ignorance and so on. The basic rights and responsibilities allow -- and to some degree encourage -- them, to socialize with one another for economic, social and civic activities. And, they allow – and to some degree encourage -- them to hold and pursue political values that define a good and just society, and to participate in shaping the rules that govern their interactions with one another.
5. As a result, individuals, making free choices about how to use their property, their labor, and their money do not only buy trinkets for themselves; they buy many things that are essential for the good life they wanted to live – one that was materially comfortable, appropriately sociable, and secure from oppression and violence from other citizens or the state. The commercial market helped satisfy many of these material needs whether they were for water, for food, for shelter, for health care, for education, for the protection of a valued religion or ethnic identity, for the advancement of a political cause, or simply to buy a greeting card that kept a relationship – a bit of social capital – in good working order.
6. Consequently, if one looked closely at the “final demand” for the many goods and services that we think of as part of the social sector -- the sector in which production systems are mobilized to produce results such as safe shelter, drinkable water, infant and maternal health, protection from child abuse and neglect, early childhood and primary education, infectious disease control, medical care for acute and chronic conditions, equal employment opportunity, safe and healthy jobs, protection against crime, the vindication of civil and political rights, etc. – a significant portion of the final demand for some particular goods and services would come from individual consumer purchases. It follows, then, that if we could find ways to increase the consumption of these particular goods at the bottom of the economic pyramid by lowering the prices, or increasing physical accessibility, or supporting financial capacity of poor individuals to buy the goods that were necessary for a good, dignified and autonomous life through market processes, then improved markets would result in improved social outcomes for all. That is why economic development is considered so important to the overall development of social welfare, and to social justice.
7. The difficulty, however, is that it is not clear that markets (as they are currently constructed, or as they can be restructured by social entrepreneurs) can be stretched far enough to ensure either the effective financial demand (i.e. incomes for the poor), or an adequate supply of the particular goods and services that seem essential to a good, dignified, and autonomous life among the poor (an effective commercially motivated supply response to the desires of the poor). If the commercial market cannot be stretched to produce levels and distributions of some particular kinds of goods and services that are viewed by individuals and collectives in society as something more important than mere wants, then some will suffer materially, and as part of their economic suffering, become oppressed and live less autonomous lives than would be desirable. Indeed, one could reasonably argue that if commercial markets could achieve the goals of ending poverty or the social and political oppression that is often both the cause and consequence of poverty, we would not have to talk about something called a social sector that sits alongside the commercial sector within a society’s social and political economy. The discussion of the social sector begins with the inability of commercial markets alone (even when aided by social entrepreneurs working the bottom of the pyramid) to meet the needs, or vindicate the rights of all those individuals currently alive.

*The Social Demand to Meet Individual Needs, Vindicate individual Rights, and Create Good and Just Societies as Well as to Satisfy Individual Wants*

1. If the focus of social entrepreneurs is to operate beyond the edges of the consumer demand to help meet the needs and vindicate the rights of individuals who are poor and oppressed to provide them with a minimally dignified and autonomous life, then the effective demand that could sustain the productive work required to meet these goals must come from something other than consumer financial demand. On this view, the demand that can support the work of social entrepreneurs, social innovators, and social change makers emerges from different motivations and takes the form of different kinds of contributions than consumer, financial demand. Four features of the demand for social innovation and change seem important to recognize.
2. The first is that the individuals who form the basis of the demand for the production of social goods, services, and conditions might think about their particular condition in society not simply in terms of *desires* or *wants* for particular goods, services, and conditions in which they live, but also in terms of what they think of as their *needs* and *rights* to have those goods and live in those conditions. Of course, some individuals are so selfish that they are inclined to view all of their *wants* as *needs* and *rights*, and to shout to high heaven when even their most frivolous wants are not treated as needs and rights that others should take some responsibility for providing to them. (I was amazed at how quickly my young children learned the difference between claiming that they wanted something to a claim that they NEEDED IT! and HAD A RIGHT TO IT!) But, one of the purposes of a socialization process (even in a liberal society!) is to help individuals: a) learn to distinguish between the things that would be nice to have, from the things that are essential to their survival, or that ensure their status in society as an autonomous, dignified human being; b) to take at least some interest in the degree to which family, friends, neighbors, and fellow citizens can have some minimal needs met, and important rights protected; and c) to understand that assuring that others needs and rights could be fulfilled might require some action that involved sacrifices from them.
3. The second is that the ideas that individuals have about the distinction between their wants on one hand, and their needs and rights on the other may, to some degree, be shared by others in the society. This is important because, as tacitly noted above, the idea that one has a need or a right to something often implies that others in the society might have some degree of moral or legal responsibility for meeting the need or vindicating the right. That is what makes a need or a right different from a mere want. If some good, service, or condition acquires the status of a need or a right, then others in the society will feel individually and collectively obligated to provide for the need or vindicate the right. But if I am walking around with an idea about a particular need or right that I have that should be acknowledged by others but is ignored, then my idea about the society in which I am living will change from one of acceptance, to one of resentment. The resentment will cause me to ask others in my position whether they have similar ideas of what a good and just society might owe to them, and if so whether they feel as much resentment as I do. If I find no response, I might have to conclude that I am simply wrong in my ideas about what I need and deserve as opposed to what I want, and accept my fate. But if I find others are thinking like me, then we might decide to organize to meet our needs and vindicate our rights as best we can on our own, or to find ways to engage the wider society in our cause.
4. Of course, individuals can and do differ significantly about what individuals are entitled to, and what other individuals would be obliged by a sense of duty to provide for them. For example, I might feel that I was entitled to a fancy car due to my long work and public service, but others would say my desire for the car wasn’t a need or a right, and that if I wanted a fancy car I should earn the money and buy it. That was up to me. It was of no concern to the rest of society. On the other hand, having just been arrested for a crime I did not commit, I might feel that I had both an urgent need and a right to a lawyer even though I could not pay for one. The society might agree that my desire for a lawyer was something that they viewed as a need and a right, and were willing to provide a lawyer to me as a matter of individual charity or collective responsibility embodied in law. But while individuals may differ on these important matters, society may need some very rough and imperfect agreement about what individuals owe and are owed by others if a life of constant disputation and resentment is to be avoided.
5. The third is that if society as a whole believes that individuals have needs and rights that need attention, then one might expect “third parties” to appear who might be willing to use their own material and social resources to meet the needs or vindicate the rights of individuals who are poor or oppressed. These third parties – the witnesses to the poverty and oppression of other individuals to whom they feel some kind of responsibility – may not have views that are perfectly aligned with the ideas of those whom they feel some moral or legal obligation to help. But, they are willing to sacrifice some of their own material, social, and political assets to provide some kind of support to their fellow human beings or citizens.
6. The fourth is that the discussion about what individuals owe to one another defined in terms of needs and rights of particular individuals, and the efforts to mobilize and deploy assets to meet the needs and vindicate the rights will happen mostly in the civil and public sectors of society rather than in the commercial sectors. It is not that there will be no discussion of needs and rights of the poor and oppressed in the commercial sector, and what consumers and producers in that sector can do to meet the needs and vindicate the rights of the less fortunate in society. (Indeed, it is precisely the hope that such discussions would occur in corporate boardrooms, and in the choices of customers, investors, and employees that gives hope to those who believe that moral commitments to corporate social responsibility might cause corporations to produce more social good and less social harm.) It is just that the discussion will more likely occur in those sectors of society that are focused on unmet social needs and rights, and that can become the third parties that can intervene in ordinary commercial interactions to change social outcomes in directions that commercial markets are not naturally inclined to go.
7. Table 1 summarizes the argument I have been making about the character of the demand side in the social sector: the particular kinds of individual and collectively created desires not only to satisfy our own individual material desires, but also to satisfy what we as both individuals and collectives are willing to view as individual needs and individual rights that make a claim on each of us as individuals, or all of us as some kind of society.

Table 1: Social and Public Valuers and Values

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Arbiter of Value** | **Objects of Valuation** | | | |
| Individual Arbiters of Value | Own Material Well Being | Well-being of Others | Moral and Legal Duties to Others | Ideas of a Good and Just Society |
| Private Collective Arbiters of Value | Material Well-Being of Group | Well Being of Others | Moral and Legal Duties to Others | Ideas of a Good and Just Society |
| Public Arbiters of Value | Economic Development | Satisfy Needs of Others | Vindicate Rights  Impose Duties | Achieve a Good and Just Society |

1. One could dismiss all the above as a kind of morality tale with little empirical reality or substance to back it up. But if that were true, it would be hard to explain a key empirical fact of our world; namely, that if one were to look at the subsectors that we associate with the idea (and the reality!) of the social sector as a whole – poverty alleviation, famine prevention and hunger reduction, the provision of clean water, infant and maternal health, reduced violence against women, primary education, etc. – one would quickly find that some portion of the effective final demand – the overall total spending on efforts to alleviate these conditions – would come not from consumers or direct beneficiaries of these efforts, but from third party payers, and that these third party payers would be paying to produce and sustain a different level and distribution of consumption of goods and services critical to ensuring a good and dignified individual life, as well as a good and just society than a market could currently supply.
2. The overall level and distribution of the production of these goods and services that each society can achieve, and the share of the cost of these goods and services that is borne by individuals paying for themselves through consumer purchases, relative to the amount that is spent by third parties such as voluntary contributors and donors on one hand, and different levels of government on the other will vary a great deal from country by country, and from sub-sector to subsector. In the United States, for example, the vast majority of the spending (the final demand) for productive activities, goods, and services that seek to educate primary school students is government. Only a small portion is paid by individual consumers. Similarly, and somewhat surprisingly, when one looks at the case of health care in the United States, one can quickly demonstrate a critically important government role in supporting the final demand for health spending. That begins with the fact that Medicare and Medicaid – programs financed directly with tax dollars – account for 37 % of spending on medical care. One can add to that the observation that much of the privately financed medical care (which accounts for 33% of total spending) consists of employer subsidized insurance which became possible only after government established collective bargaining rights which allowed workers to bargain successfully with their employers to include health insurance as part of their compensation. And, one could even treat the mandate imposed by government on individuals as part of ObamaCare that required them to purchase insurance from private insurance companies as government demand for health insurance. Only 12% of health care spending in the United States comes directly out of the pockets of consumers.
3. As an important empirical fact, then, the effective demand – defined in terms of the human aspirations and values that are used by individuals, voluntary associations, and polities to: a) evaluate the quality of their individual and collective lives; b) motivate individual and collective action to improve those conditions; and c) generate revenue streams that support the collective efforts of the producing organizations that make up the supply side of the social sector – comes not just from consumers spending money on their wants, but also from d) individuals making voluntary contributions of money, labor and voice, and e) polities deciding that they are willing to tax and regulate themselves to meet both the individual desires of those who have needs and rights but cannot accomplish that with their own resources.
4. In fact, as noted above, we might treat the presence of moral and financial demand for productive activity from third parties as *the defining characteristic of the social sector*. If all individuals in society were able to satisfy their needs and vindicate their rights (as both they and others in the society saw them) by paying for the production of these conditions, we would not have to talk about, or help to create and shape a social sector: we could leave everything to the workings of the market. It is only *because* the market, *as currently operating*, will not necessarily produce social conditions that provide for individual needs and vindicate individual rights as we individually and collective define those needs and rights that we have to create something other than a market driven by individuals with money to spend to satisfy their own wants, meet their own needs, and vindicate their own rights. We create a demand for the improvement of individual and collective social improvements that expresses itself normatively and financially through the actions of voluntary contributors, and citizens making choices within and through civil society institutions, politics, and government that are consistent with their ideas of a good and just as well as prosperous society.
5. In retrospect, it should not be surprising that “consumer demand” alone would not be able to guarantee that important new ideas in the social sector could scale to significance. After all, much of the social sector was focused on helping those who were particularly impoverished and oppressed, and whom markets had not reached to transform their conditions because they had no money, and no effective power to turn the producing sectors of society in their direction to meet their needs and vindicate their rights. But a key conclusion of this analysis is that if we want social sector firms and industries to work like commercial sector firms and industries, we have to pay close attention to the demand side of the voluntary sector as well as the supply side, and the demand side in the social and public sector operates differently than the demand side of a consumer market.

*Tapping into the Demand from Voluntary Donors and Government for Innovation and Scale*

1. If third party payers – voluntary contributors and government – are important parts of the effective final demand for generating improvements in social conditions because individuals with money to spend on their own welfare, their own needs, and their own rights do not create either enough, or an equitable distribution of effective final demand, then we have to think through the question of how social entrepreneurs can overcome this key limitation, and make the best possible use of voluntary contributors and government in developing and launching their ideas, and scaling them to significance.
2. One way to think about this is to make visible the critical difference between the kind of financial support one needs for start-ups, and the kind of financial support that is needed for scaling to significance. Table 2 presents a very simple diagram that distinguishes between investment capital to get things started, and revenues that are necessary to sustain and scale an enterprise to significance. It also distinguishes among these activities in the private, voluntary, and government sectors.

Table 2:

Sources of Financing for Starts and Scaling to Significance in

Social Entrepreneurship, Social Innovation and Social Change

|  |  |  |  |
| --- | --- | --- | --- |
|  | **Commercial Markets** | **Philanthropic/Voluntary Sector** | **Government** |
| *Start Up Capital* | Commercial investing at market rates of return | Foundation grants (with or without performance goals) | Social research and development funds |
| *Funds to Support Scaling and Sustaining at Social Impact Level* | Consumer Revenues | Leveraged by other foundations  Find commercial market  Policy advocacy for government financing | Government financing through grants, contracts, entitlements, vouchers |

1. Using this simple table to frame my critique, I would suggest that we have been acting as though the principal problem that the social sector faced has been in finding enough social entrepreneurs with new ideas, and finding enough social venture capital to get them launched. (I am assuming that the commercial markets continued to operate with some impact on social conditions as well as individual welfare.) Fortunately, that problem could be quickly solved by increasing the level and changing the nature of philanthropic giving – particularly the practices of large philanthropists and foundations.[[2]](#footnote-2) Much of the emphasis was on the cell in this matrix that captures the activity associated with developing and launching new ideas – primarily with support from philanthropists.
2. The simple fact that social entrepreneurs cannot rely simply on consumer demand in commercial markets to scale their good ideas but would eventually have to rely to some degree on government sources of funding can go a considerable distance in helping us understand why many social entrepreneurial efforts have stalled at levels well below the ambitions of the entrepreneurs themselves, or the claims of those who were the champions of their movement. But to understand what might be necessary to *improve productivity* in the social sector, it might be important to dig a bit more deeply and look more broadly at how the demand for social change could actually perform the functions that Schumpeter assigns to the demand side. We will return to the question of whether there is adequate effective, financial demand in society to meet the goals of poverty reduction and the reduction in social and political oppression later. For now, however, it is useful to return to the role that demand plays in: a) motivating social entrepreneurs; b) in helping them identify the particular value creating activities that could help them achieve their goals; c) in testing the value of the ideas that are created; and 3) to align the good ideas with money tied to the production of social goods at a scale that would make a difference.
3. What we will see is that while the image of social entrepreneurship has done a great deal of good in raising questions about the conditions that could support dynamic efficiency in the society sector of societies, it has focused much too much of our attention on the institutions, motivations, and processes of commercial markets, and not enough on the institutions, motivations and processes of the civil, political, and governmental sectors of society.
4. To be sure, we will find that there is much work to be done in invigorating these institutions and processes. But unless we find ways to include the civil and public sectors in the task of improving the performance of the social sector enough so that we can expect to see improvement in this sector at a price we can stand to pay in the next decades, we will likely fail. If the market sector acting alone driven by consumer demand and profit driven firms could have given us not only prosperous, but also good, just, and sustainable societies, presumably it would have done so.

*The Social Demand for a Good and Just Society and the Supply of Entrepreneurs*

1. In Schumpeter’s model a critical input to a system of production that can produce dynamic efficiency is the supply of entrepreneurs with good ideas about how to improve the performance of the existing supply system. The supply of entrepreneurs with good ideas, in turn, is produced by individuals who would like to make money from the invention of a new product or service, the existence of a latent financial demand that can plausibly be tapped for large scale, sustained revenue flows, and the supply of sufficiently venturesome and wise capital markets that can support the entrepreneur through the long process of developing and fielding a valuable new product or service.
2. The set of structures and processes that have supported these efforts have done very well in attracting large numbers of individuals with value creating ideas to develop new products and services that consumers really liked, and along the way, made them considerable fortunes. They have also, no doubt, swept up many individuals whose motivations were not strictly mercenary, but included other motivations such as the pleasure that comes from solving a technical problem that no one else had solved, or in envisioning a future in which problems and tasks that individuals at all levels of society found burdensome could be made less so through some new invention, or simply finding something that could add pleasure to life. That stream of ideas not only grew the economy, and produced jobs and much higher standards of living for man y, but also helped to deal with problems that would otherwise have persisted as social problems (such as even more extreme poverty, or a healthcare system that had no live saving drugs to provide to patients).
3. But, again, what is interesting and distinctive about the idea of social entrepreneurship, is it is fueled in large part by the desires of individuals, now described as social entrepreneurs, whose principal motivation in launching a producing enterprise is to make a change in social conditions. They have to worry about having enough money and voluntary effort to sustain the productive effort, but their principal goal is to change material conditions in the direction of material well-being for the least advantaged, and more equal social and political status for all, but particularly the oppressed. . Importantly, the desire is not only to see a change, and enjoy it when it has occurred, but also to *make* the change through highly leveraged individual action. It is at that moment that the demand for social change becomes the supply as well.
4. If social entrepreneurship begins with individuals examining their own situation and that of others in light of the conditions they view as necessary for a good life, free of economic, social, or political oppression, then it should be clear that social entrepreneurs could come from many different locations in society. It could include individuals in the economic sector, but also those in civil society, the voluntary sector, politics, -- even government officials. It could also include individuals at many different levels of society ranging from elites, through ordinary folks, to those currently at the bottom of the economic, social or political hierarchy.

*Developing Social Entrepreneurs and Innovative Ideas in All Sectors*

1. This last observation suggests that some of the most important social entrepreneurial activity might well come from the particular populations that are actually experiencing the conditions that seem intolerable to themselves, and to their similarly placed fellows. Indeed, one could observe that even if poor individuals did nothing more than produce an ordinary commercial enterprise that provided valuable consumer goods to poor individuals at a fair price, and employed poor individuals in ways that provided a decent wage and respected their rights as humans, then the enterprise could reasonably be viewed as a social enterprise. What would be particularly valuable, and particularly social, is that such entrepreneurs used their detailed knowledge of the conditions in which they were living to figure out exactly how those conditions could be improved through methods that neither the market, nor the suppliers and demanders in the social sector had yet discovered.
2. Finally, if the suppliers of new ideas to deal with problematic social conditions are also the demanders of those innovations, then it is at least possible that many important ideas could get started from many different locations in society fueled by nothing other than the vision and values of socially alert and concerned individuals. To shift to a popular social ecological idea, the seeds of social change might already be distributed widely across the ground of social action. All that is needed some rich soil, some sunlight, and some rain to start the growing. This is why the search for social innovators and innovative ideas has to look across all three sectors, not just one, and at all levels, and in various subsectors defined by social conditions being experienced by particular populations. That is the genius of a liberal democratic political economy. Social innovations can start, and perhaps begin to scale, from any social location.
3. We know from the study of entrepreneurship in the commercial sector that new ideas need a period of “incubation” to have a chance of succeeding. This period is a necessary part of developing a new idea -- perhaps even in adapting an established idea for some new local situation where the idea has not yet been tried. But that period can take two quite different forms: it can simply be a cold bath during which those with ideas are struggling with nothing more than sweat equity, and the help of a few friends, and financial support from families; or it could be carefully incubated with financing and technical assistance from those who have helped others along this journey.
4. We do not know for sure, but we assume that many ideas for making social change could benefit from some kind of incubation with social, financial, and technical support. The private sector, operating through venture capital operations, have learned a great deal about how to “incubate” commercial ideas. Many venture philanthropists have sought to extend these practices into the world of social change entrepreneurs. Their methods include not only finding promising new ideas, but also finding promising individuals who seem to have the desire and capacity to succeed in making social change, and then supporting them as individuals, not just their ideas. This approach has produced some notable successes. But important questions remain about the question of whether there are implicit biases towards some kinds of social change efforts and away from others in these institutions. These implicit biases could emerge either from systematic biases about the ends and methods used by social entrepreneurs, and/or from weaknesses in the analytic methods they use to estimate the ultimate social change potential of ideas they are considering.
5. Given these concerns, it is perhaps encouraging that there are other sources of “risk capital” and other ways of helping social change ideas to scale in both civil and political life. Traditional foundations have long provided funds to support basic research on the character, extent, and dynamics of social conditions that many would describe as social problems to be solved. They have also supported applied research to develop and test particular interventions designed to ameliorate the problems. They have also found and supported unusually creative individuals whom they hoped would produce important new knowledge, promising interventions, or actual social change.
6. Government, too, has developed its own methods for promoting innovation and social change. It is easy to forget that democratic elections provide a regular opportunity for those with better ideas about how to solve social problems using government assets to put their ideas before the public. In this sense, politics is a friend rather than an enemy to social change insofar as it allows people with new ideas to compete for the control of public assets. (The worry, of course, is that the innovative ideas will turn out to be nothing more than new labels for existing practices, or promises that are not kept, or big ideas that turn out not to work very well.)
7. Beneath the level of electoral politics, however, government supports a great deal of both basic and applied research that can stimulate the development of plausibly effective interventions in dealing with specific social problems. Indeed, it is easy to forget that it was the government that helped transform America into a great agriculture and mining nation through the development of the system of land grant colleges that supported the development of these industries across the nation; equally easy to forget that basic and applied research in physics and biology have provided the underpinnings for success in the industries that rest on both basic and applied knowledge developed within these scientific fields.
8. More recently, as part of the movement to encourage social entrepreneurship and government innovation, governments have begun experimenting with special offices, funding mechanisms and management processes to create innovative approaches to solving social problems. Some of these improvements lie within improved processes within a given organization. Some depend on more effective operational co-ordination across government organizations. And some involve innovations in governance that cut across organizations located in different sectors, and sweep up their existing capacities in an effort that can outperform what they were previously doing.
9. As noted above, it seems quite possible that the range of efforts made to increase the number of ideas and entrepreneurs has outstripped our capacity to test and diffuse the most promising new ideas. Also as noted above, it is when one seeks to dramatically increase the scale of new social change ideas that one must often come to grips with government, since it is government that controls much of the spending for many important social change activities. Therefore, when one comes to the challenge of scaling good social ideas, one must deal with the way that government tests and decides what is valuable to do. It is these processes we explore below.

*Sizing Up “Problem Spaces” ( Rather than “Market Spaces”) for Social, Entrepreneurial Action*

1. Key to the success of entrepreneurial efforts to improve productivity in the social sector is the capacity to identify the particular problems that need solution, and the development of ideas that can outperform current efforts to deal with that particular problem. This is analogous to the challenge that commercial entrepreneurs face in developing a new product or service that can compete for consumer attention in an existing market. If they cannot develop a better mousetrap (or at least one that is cheaper or for some other reason more satisfactory to customers), then their effort will fail, and with that a failure to improve the productivity of the mousetrap industry.
2. The analogy is an imperfect one, however, because the technical challenge facing social entrepreneurs is not to find a “market space” (defined by consumers with wants and money to pay to satisfy them); but instead to find a “problem space” (defined by a socially or publicly defined need or right which third party payers – as well as client beneficiaries are willing to pay) for which they have a more effective, lower cost solution.
3. In the typical case, a problem space is defined in terms of a particular feature of the physical environment (both natural and man-made) that is viewed as threatening or problematic in some way, or a part of the social environment in which particular populations of individuals are living in materially disadvantaged, and/or economically, socially, or politically oppressed conditions. That particular condition becomes a social problem *when individuals in the society, and voluntary associations of individuals, view it as such*. The dissatisfaction produces a flow of voluntary effort and money, as well as social and political pressure for government to use its assets to deal with the problem.
4. Social problems can be viewed as more or less significant, and more or less urgent. The *significance* of the problem can be assessed in terms of both the number of individuals affected, and the magnitude of the disability those individual experience. The *urgency* of the problem is importantly related to its size and significance, but is also related to the *dynamics* of the social condition that has been identified as problematic. If a problem is quickly deteriorating, and there are actions that can be taken now to prevent it from getting much worse that will be useless if one waits, then urgency increases. Generally speaking, the more important and more urgent the problem, the more resources will likely become available to solve the problem. But the link between social conditions that require significant or urgent attention, and the mobilization of resources to solve it may be much less than perfect.
5. The flow of resources to solve or improve a social problem depends not only the importance and urgency of a problem (viewed both objectively, and by members of a society within which the problem exists), but also on the idea that some solution might be available. If a problem cannot be much improved, it might be best to view it as a condition to which the only useful response is to learn to adapt to its presence. If however it is a problem that can be improved, then it might be easier to mobilize resources attached to the particular solutions.
6. As noted above, a key task for social entrepreneurs is to not only see and publicize (market?) the existence of a social problem, but to develop plausibly effective interventions that could solve the problem. This is roughly analogous to designing the new products and services that can better satisfy demand in a consumer market. But again, the analogy is imperfect and potentially misleading.
7. The key analytic tasks in developing a new product or service in the commercial sector are: a) to carry out a market analysis of what particular product or service, and what particular attributes of that product or service are valued by consumers; b) to design a product or service that has the particular bundle of desirable attributes that will appeal to consumers; c) to design a production process that can produce the bundle of attributes at low cost; and d) to design a marketing strategy that puts the new product in the front of customers’ minds, and within easy reach of purchase. Exactly what has already been learned or considered about these matters, and how an enterprise will move forward on these fronts is the core technical content of what is called a business plan.
8. The key analytic tasks in developing an improved response to a social problem is generally the same, but in particular quite a bit different. The starting point is not a marketing analysis of a consumer market; it is the representation of a social condition that is the target of change, along with an analysis of how big and urgent the problem is, and a review of what social actors might be poised to provide the energy, material resources, and money to solve it.
9. The second step is to design an action that could be taken by some particular organization (or set of organizations) that could be plausibly effective in changing the target social condition. That activity – defined as a set of organizational outputs – may have many different elements, each of which could turn out to be important in producing the desired social results. Often, both existing social science knowledge and particular social science methods have to be used to design and test the particular attributes of an intervention that are the “active ingredients” in producing the desired changes.
10. The third step is to design a production process that can produce the particular outputs that are thought to be “adding value” to the effort to solve the particular problem. This may be relatively easy to see in efforts designed to produce changes in physical conditions. But when one is dealing with social conditions through the use of combinations of products and services, it is often more difficult to discern and design for the most important active ingredients. The reason is that the processes of delivering the services is often indistinguishable from the attributes of the service being delivered that produce the result: the process is the output that produces the desired result.
11. The fourth step is to figure out which segments of the population now suffering with a particular condition should be the focus of the social change efforts. This is often a very difficult decision to make since there are two different answers to this question that make different trade-offs between efficiency on one hand, and equity on the other. The principle of *efficiency* would direct the social change agent’s attention to the populations that could take greatest advantage of the intervention being rolled out. That might well include individuals that are actually doing pretty well, and close to the line that society is using to distinguish those particularly in need from those who are doing ok on their own. The principle of *equity* might push in different directions: either in the direction of providing equal services to all who are suffering with a particular condition regardless of their ability to take advantage of the goods and services being provided to improve their own lives, or even to those who are most disadvantaged on grounds that the principle of justice requires that special effort be made to improve the conditions of the “lease advantaged” in society in an effort to raise the minimum floor for individuals living in a given society.
12. This process looks much more like the process of policy analysis or program design as it is carried out in foundations, in governments, and in schools of public policy and management than it does like business planning. The result is not so much a business plan that explains how a particular product or service can be inserted in a given consumer market and generate revenues above costs (profits) over a given period of time as it is a “social value proposition” that explains how a particular intervention launched by some particular enterprise could be expected to improve a given social condition experienced by a given population over time. The key question here is not what can be produced that folks will buy, but what can we produce that would move the needle on some social condition we, along with others, viewed as a problem.
13. These techniques are different from those used in business planning. But as in business planning, the proposals that emerge, and those that are taken up, will vary along predictable lines. The most obvious is that the proposals can differ a great deal in terms of the size of the initiative that is being proposed. Note that the size of the initiative is probably not necessarily the same as the size of the problem, since many new ideas are not well enough tested to be rolled out at a scale that would solve the whole problem. It is important in assessing the value of a proposed initiative to see the potential of the idea for scaling to significance if it works. But at the outset, the initiative will be much smaller.
14. Note also that the size can be measured in many different ways: an investor could look at the current cost, or impact at proposed scale, or impact at a predicted future scale that is more or less feasible. But size could also be measured in terms of the complexity of the initiative that is being suggested, and in particular, the number of organizational and sector boundaries that have to be crossed in developing the proposed innovation. The institutional complexity is important to consider in part to assess operational risks in executing the effort. But institutional complexity – defined in terms of organizational boundaries to be crosses – also has a significant impact on the level and kind of legitimacy, support, and authorization a social entrepreneur will need to successfully mount and execute the proposed change – even if the initial proposal is small in scale.
15. By definition, all proposed changes in approach to dealing with a social problem are risky. The reason is that the innovators do not know exactly what will happen. This is less true if one is transferring or adapting an innovation that has been tried elsewhere to a new location. But even in this case, there is some risk to the “early adopters.” Consequently, the array of innovations proposed by social innovators that will actually be tried depends a great deal on the risk tolerances of those supporting the innovation. We can follow all the analytic steps above to reduce the risks of failure (or, even worse, making conditions worse than they otherwise would have been). But even if we are careful and brilliant analysts, we cannot eliminate all the risk.
16. This might be particularly important for the social sector, because government might be considerably more risk averse in supporting new ideas than either the commercial sector, or the voluntary sector. To many citizens and taxpayers, it seems wrong to “gamble” with other people’s money – particularly if the gamble includes the possibility that an outcome could be worse than what could be produced with known methods. It may be for that reason that liberal societies have depended more on the private sector – commercial enterprises and venture capitalists, and nonprofit organizations and philanthropists – to support the risky work associated with assessing the size and nature of problems that are not captured reliably in our national data systems, or in developing and testing new approaches to both old and newly discovered projects. But it would be a mistake to ignore both the large investment that government does make in horizon scanning activities, in basic sciences that help us understand basic causal mechanisms, and more applied activities focusing on developing and testing interventions. But as Table 2 reminds us, the government also engages in important innovations. Indeed, some of the riskiest investments in the development of basic knowledge of both our physical and social world are made by government. We could hardly begin to even see, let alone solve social problems without the large investment that government makes in monitoring and responding to aggregate economic, social, and political conditions.

*Testing the Ideas for Value is a Challenging Task*

1. The best test of whether a new idea for dealing with a social problem can outperform an old idea is to try the idea and see whether it works better than what we did in the past. In the commercial sector, that is relatively easy to do. All one needs is offer the new mousetrap for sale, and see whether sales take off or not. One may have put a lot of effort into designing the mousetrap to work better on many different attributes of quality that consumers might demand (e.g. low cost, ability to attract mice in the vicinity, little pain and suffering for the mouse and easy disposal if the mouse is killed, or simply effective immobilization for later relocation if the mouse is captured alive, etc.). But the test of whether one has designed a better mousetrap is ultimately whether individuals buy it. That decision to buy contains within in both a judgment of functional utility in producing results, and the particular attributes of value that are important to consumers.
2. In the social sector, tests of whether one has better method for dealing with a given social problems is a more difficult – and slower and less objective – process. The difficulties begin with the fact that judgements as to efficacy and value of the intervention often have even more particular dimensions of value to consider than consumer products and services. When we ask whether a particular intervention to reduce “homelessness” has been effective or not, we might begin an apparently simple effort to reduce the number of nights that individuals slept “in the rough” in a given geographic area. Presumably, that number could be reduced by providing some kind of shelter that would allow those with no place to stay to find a roof and some warmth. That effort might quickly be expanded to characterize key aspects of the shelter provided such as: the amount of space and privacy afforded to each individual; the safety of both people and property in the shelter; the amount of time the shelter was available for use; the length of stays that would be allowed for residents, etc.
3. It wouldn’t take long to go from those attributes of the service to consider whether the array of services that could and should be offered to the residents should be expanded to include screening for medical and mental health problems, checkups on whether the residents are complying with drug regimens, referrals to employment opportunities, etc. Each of these attributes of the intervention to deal with homelessness could be viewed as valuable in its own right (the specific services provided could probably be valued in the market), but also as means towards a potentially more valuable end – a reduction in the extent to which particular individuals had to rely on the services provided in the homeless shelter on one hand, and a reduction in the aggregate size of the population that was still sleeping rough, or predominantly reliant on shelters.
4. The fact that any particular intervention can (and will!) be evaluated by the clients, the donors or volunteers who have contributed voluntarily to the effort, or citizens and taxpayers who have agreed to tax and regulate themselves to produce this intervention, means that the task of measuring the results observed will be difficult for no more complicated reason that there are many different attributes of performance that matter to those who have an interest in the way the intervention of performing. But beyond the fact that there are many different dimensions of value lies the additional fact that many of these other dimensions are conceptually hard to define and measure. To some degree, we can measure the quality of the service through client surveys, or client complaints about conditions. But, if we want to be sure that were are providing a quality service, we might have to make regular inspections of actual conditions in the shelter against some standards of privacy, cleanliness, security – even hospitality. And, if we want to produce some broader, long range effects on the residents so they don’t have to keep returning, we need to monitor not only that they are getting the help they need, but also that the help is provided at a level and in a way that actually produces results. Essentially, to discover whether a particular intervention “worked” or not, we have to decide philosophically what was the value we were trying to produce, do the political work of aligning those values with the values of the various stakeholders who are financing, evaluating and using the services, engage in the technical task of developing and testing measures of the degree to which those values are achieved by or reflected in the operations, and then find ways to use those measures to demand and get a consistent performance, and to find ways to keep improving. That is a lot more work than simply waiting to see whether consumers buy the new product or service.
5. The fact that we are often interested in impacts on individuals that occur down a causal chain into the future that results in their “natural condition” improving or continuing to be bad creates the additional problem that we often need to wait to see the impact on the individuals. And the fact that we are interested in seeing the degree to which a particular intervention, or even a particular set of interventions has dealt adequately with the problem at scale, we have to keep track of the condition not only of those who have been part of the program, but also the wider population who experience the problem, but are not now known to the system we are operating. These requirements impose additional burdens on the measurement and reporting systems that can tell us whether a particular intervention is or is not work at all, or better than the alternatives available to us.

*Aligning Money to Value is Also Hard*

1. Ultimately, efforts to improve productivity in the social sector have to depend not only on the supply of entrepreneurs with good ideas, and the skill and commitment to pursue them; and not only on the quality of their analysis of problem spaces and the development of plausible solutions to old or emerging problems; and not only on the empirical tests of whether a good idea actually works to achieve the desired results; but on the capacity of the system to align the big money that is devoted to supporting solutions to problems at scale with the ideas that seem to work. If many ideas that work are developed, but we continue to spend money on what doesn’t work, all of the effort that went into innovative entrepreneurship will be wasted. If the systems we rely on to distinguish the ideas that work from the ideas that don’t are easily fooled by fraud, by fads, or an excess of optimism, then the entrepreneurship in the field will lead to bad rather than good results. So, much depends on the discrimination of those who will come in behind the entrepreneurial efforts to make the big commitments to scaling a few of the new ideas that are on offer. They need to be reliable arbiters of social value, and reliable judges of which ideas really work to produce that value.
2. In the commercial sector, we do not need to worry too much about aligning the funding to scale commercial innovations to significance. Since consumers are providing the revenues needed to scale, and they are recognized as the appropriate arbiters of the value of commercial products and services, by definition, the money flows to the “best” ideas. In the social sector, however, where much of the funding for both innovation and scaling will come from third party payers such as voluntary donors or government, the question of whether the voluntary donors and government are “good” arbiters of “social value”, and whether they have the interest, information, and discipline to align their investment and (more importantly) their large scale expenditure decisions with activities that actually produce important social outcomes at a reasonable price is a more problematic issue.
3. One key question is whether the interests and concerns of the third party payers are adequately responsive to and aligned with the most urgent and important social problems. This is essentially analogous to the question of allocative efficiency in the commercial sector: whether resources and productivity activity are focused on producing the products and services that consumers want. But, as Table 2 suggested, when we turn to the “social sector”, we assign the important task of assigning social value to particular activities to three quite different social actors.
4. First, we give the responsibility to individuals acting in the role of philanthropists, donors, or volunteers who use their rights to use their own resources in any way they want to use some of those resources to try to alter social conditions in a direction they judge to be valuable. This can produce some highly varied and idiosyncratic judgments. (One frustrated child advocate once noted that it was easier to raise money to protect pets than it was to raise money for disadvantaged children!) But we are prepared to put up with the idiosyncratic judgments about social value for both principled and practical reasons. Just as we are willing to accept consumer judgments about the value of pet rocks, we are willing to accept donors’ judgements about the importance of animate pets as a part of our commitment to individual liberty – as long as the donors are using their own money, and are not doing anything that threatens the rights or well-being of others. We also can imagine that idiosyncrasy can, on occasion, draw attention to conditions or problems that had not been the focus of attention, but once noted, might attract public attention and make the problem seem more socially urgent and important, and less idiosyncratic. The freedom given to individuals to think on their own, and act to solve social problems can be a dynamic force in social efforts to scan the horizon for problems we have not yet seen or taken seriously enough.
5. Second, we give the responsibility for deciding what constitutes a social problem to civil society associations. By definition, these organizations that act voluntarily on behalf of identifying or solving social problems experienced at individual or aggregate levels are less likely to hold completely idiosyncratic views of what is socially valuable. After all, they have attracted others to a shared vision of what they could do to make the society better or more just. They may also have more economic, social, and political power than the average individual (though not necessarily less than very wealthy philanthropists). Both the fact that their views have had to meet the test of gathering others into the tent, and that they have more votes, more friends, and more money to deploy, and can establish them as important arbiters of social value as well as individuals.
6. Third, we give responsibility to the processes of politics and the structures of government to spot potentially urgent and important social problems, to decide how important they are, to decide who might have both the moral or legal responsibility and capacity to act to deal with the problem, and then to orchestrate the social actions that could plausibly improve or solve the problem. There are two key differences between the processes of politics and the policy decisions of government on one hand, and the processes of individual or collective voluntary action in defining social problems.
7. The first is that when we engage in a political process, or a governmental policy making process, the anticipated result is a decision to use the assets of the state to solve the problem. The assets of the state include both: a) the direct authority to require private actors to refrain from socially harmful acts and to engage in socially beneficial acts; and b) the use of public dollars (raised through the taxing power of the state) to produce desired social outcomes.
8. The second is that the authorization to use those (collectively owned assets) requires a collective decision – a choice made by citizens and their elected representatives acting through the messy processes of democratic governance. Individuals do not arbiter the value of the particular choice; a collection of individuals, linked to one another through their citizenship in a state, make the decision as to social value through a complex process that (more or less unsatisfactorily) aggregates individual ideas about what they want for themselves, and what they want for others, and how they would like to use their government to create a prosperous, sociable, and just society.

1. The process of building a “we” that can agree to tax and regulate itself to accomplish particular social goals is a difficult one. That means that the process can be very slow. Moreover, once the decision is made, it is made for all. That means that that the collective choice that is made will not have much individual nuance. Slow, cumbersome, and crude doesn’t seem consistent with the ideal of a fast, responsive, and tailored response to social problems that we might hope to see in a vibrant social sector. In that kind of social sector, government would be trying many different approaches to improving social conditions. Some of those might be effective in dealing with niche problems in particular locations. But others might be more robust and work well across many different circumstances and places. If we think of government as an inflexible monolith, the advantages of trying many different methods to find some that work will be hard to expect.
2. But these observations ignore the fact that neither politics nor government is a hegemon that is incapable of acting quickly, or producing variety in its actions. As noted above, popular elections are often occasions for new ideas both about problems to be solved and methods to be used to be developed and tested. Similarly, most liberal governments have some decentralized units that are free to experiment with their own aspirations, their own money, their own judgments as to what are important public values to be pursued, and their own preferred methods for pursuing those goals. This is the important insight that lies behind a vision of state and local governments as the laboratories of democracy – the place where differences can lead to new ideas and generate experience that can be used by others. And many government activities are staffed by professionals whose commitments and credentials encourage them to try to improve the efficacy of their methods – whether those be in health care, civil engineering, social work, education or policing. So, there are many spaces and drivers of innovation in politics and government. The challenge is not to ignore these, but to improve them.

*Towards Improved Government Capacity to Support Social Innovation and Social Change*

1. As noted above, for many efforts to solve social problems – particularly those that require lots of effort to change the material conditions and life trajectories of those who have long been at the bottom of the economic, social, and political ladder – much of the money for developing and sustaining a new idea at a scale that could make a real dent on the problems we face will probably involve government dollars. By definition, the client beneficiaries of these programs are not likely to be able to pay the full cost of the benefits and services they receive (though there may be no reason that they couldn’t pay some.) Voluntary contributions of money from large and small donors, and voluntary labor contributed by volunteers can go part of the way in closing the financial (and labor) gap, but it is hard to sustain philanthropic and voluntary giving at a high enough level, over a long enough period of time, to make a significant impact on the communities in which we llve. It is left, then, to government to finance and otherwise support the large, sustained efforts to solve social problems.
2. This may come as bad news to those who were hoping that social entrepreneurs could reduce the need for government in dealing with problematic social conditions. Yet, in thinking about the role of government in dealing with social problems, one should distinguish between the idea that we don’t need government *agencies* to *produce* the desired social results, from the idea that we don’t need government *financial, legal, and moral support*. It is this idea – to separate government production of social goods, services and conditions from the government financing of the efforts of commercial and non-profit organizations to produce these conditions – that has fueled a significant shift in government practices towards the privatization or marketization of government efforts to deal with social problems, and has created some room for social entrepreneurs to enter on the supply side of the social sector. One could be eager to introduce a more entrepreneurial element to those engaged in productive efforts to make important social changes without necessarily assuming that we would be able to dispense with government financial support in the successful improvement of social conditions.
3. Indeed, in thinking about how government might best participate in generating productivity gains in the social sector, one might begin with the idea that “intrapreneurs” in government might be given more leeway to use their imagination, and professional knowledge to generate and test innovative ideas as well as the social innovators in the private commercial or voluntary sector. But if the hope for “bureacractic entrepreneurship” seems remote, one can quickly turn to the wide variety of ways in which government financial support could be used to support innovative start-ups in the social sector, and, perhaps more importantly, to scale them to significance by shifting government expenditures on technically inefficient and ineffective methods for improving social conditions to the more effective methods developed by the social entrepreneurs.
4. One can easily see government, acting with its financial resources, its regulatory authority, and its moral leadership (if any such remains!) as an important “market creator” for combined social action in the “problem spaces” where social problems can be found. The financial instruments government can use to “make” or “shape” the market for improved social performance include all of the following:
   1. It can provide direct funding to research and development in different social sectors in the search for improved methods for dealing with social problems
   2. it can provide direct funding to both commercial and non-profit enterprises that can contribute to the solution of social problems.
   3. It can provide tax-financed vouchers to individual clients and beneficiaries of social sector organizations.
   4. It can reduce the financial risks and capital costs of an organization by insuring it against certain kinds of risk at a low cost.
   5. It can reduce tax burdens on organizations operating in the social sector.
   6. It can reduce taxes on those who contribute money or time to organizations working in the social sector.
5. All of these forms of financial support now exist, and are presumably producing important effects on the shape of the various supply side enterprises that seek to provide public goods and services, or improve social conditions in some way. But whether and how these different forms of government financial support can be used to stimulate improved performance among the social sector firms and industries that constitute the social sector – how the government can support social entrepreneurial efforts scale to social impact and significance – is one of the important questions facing both social entrepreneurs and government policy makers in the immediate future.
6. Key to the success of such efforts will be the development of measures that can reliably record the impact of social enterprises working to solve social problems at both the level of individual firms, and at the level of the society as a whole. Measurement of performance at both firm and aggregate levels is important for at least three reasons. First, to the extent that we are serious about actually trying to ameliorate specific social problems as they appear across the society as a whole, it is important for us to have some way of estimating whether we have had an impact on the problem at scale, or only as a partial solution, or much worse, nothing more than a gesture.
7. Second, due to the heterogeneity of problems and populations even when defined in terms of particular sub-sectors of social problems such as chronic diseases among the elderly, or educational services for youthful offenders, it is quite possible the processes of social innovation will generate solutions to some part of the problem, but not the whole. In order to see the progress that we have made, and the work that remains, it is important to be able to distinguish between the solution of niche problems and the solution of more general problems. To do that, we have to be able to see the niches in the context of the more general problem space.
8. Third, to the extent that what first appears as a promising solution to a niche problem might in fact be close to the solution for the more general problem, we have to be able to see in the niche solution the potential for making rapid strides in scaling up to a more general solution rather than getting stuck in a niche.

*The Path Forward:*

1. These observations point towards the need for a significant shift in our thinking, and the development of a much more demanding form of analysis than we have so far relied upon.
2. On one hand, we almost certainly have to give up our confidence that the important social change ideas currently being developed by social entrepreneurs can be scaled to significance through the power of consumer demand alone. If they could, presumably the market would have already found and exploited these opportunities. All that would be needed is just a “nudge” from society as whole to be on the lookout for activities they might carry out, or products and services they might produce and deliver, or environmental and social conditions they might be able to produce that would be socially (if not financially valuable) that they could do at low cost. For those social conditions that individuals and collectives in society define as social problems that do not generate an effective consumer demand because the individuals experiencing the conditions lack both the money and the status to demand improvement on their own, third party payers and supporters will have to carry the load. The third party payers include both voluntary contributors, and government acting in response to political pressures from citizens who want to use the government to help create what they see as a good and just society by dealing with particular social conditions they view as problematic. This means that many, if not most, social entrepreneurs will have to figure out how to build on their own (or to take advantage of somebody else’s) efforts to create social and political movements that can generate the demand (along with the supply!) of productive enterprises that can actually improve social conditions.
3. On the other hand, we will have to become much more knowledgeable than we now are about how the somewhat unusual supply and demand conditions that exist in the social sector that include commercial, charitable, and government suppliers and producers; commercial, charitable and government investors and purchasers; and commercial charitable, and government arbiters of the value that is being produced in the sector combine to support or undermine the key purpose of producing sustained productivity gains in the social sector. We have already taken the important step of recognizing that at least some, maybe a great deal of the final demand for the work of the social sector will have to be financed by government. but that leaves unspecified how these different sources of production, financing, and valuation can best be combined to produce a dynamically efficient social sector.
4. This means we have to look more closely at the particular structures and processes that are supporting the current dynamic elements of the sector, and what it will take to enhance the speed, power, and quality of those dynamic elements, as well as what can support the sector as a whole. It is fine to say that “entrepreneurs” are doing the work. And it is great that we think we can rely on creative, dedicated individuals to do much of the work on their own. But in order for this to yield steady productivity gains in the social sector as a whole, we have to look much more closely at the processes that support the development of innovative ideas, the particular ways they are tested, and the processes that ensure that ideas that work will grow, and those that do not will fall by the wayside.
5. A path to explore here would be to recover the methods of industrial organization from economics. That now neglected field took its original inspiration from Schumpeter in the sense that it was particularly interested in the question of the degree to which particular industries could be relied upon to produce significant productivity gains over time. That was the way that industrial performance was defined: was the society benefitting from the forces that Schumpeter had identified as essential to motivating dynamic efficiency. That theory was tied to a particular idea about how the structure of an industry could affect the rate of innovation; namely, the more firms, and more competition, and the easier it was for new firms to enter particular markets, the more dynamic the industry would be.
6. But the theory also took account of what was described as the conduct of the firms in the industry as well as the basic structure. By conduct, the theory referred to the particular corporate strategies that were being pursued by each of the firms in the industry. For the most part, the assumption was that firms would behave competitively, and seek to develop and hold onto particular market niches that would allow them to earn profits above the industry average. They might also work very hard to increase their scale to enjoy what economies of scale were to be had in their particular enterprises, and to increase their market share so they could begin to enjoy some of the benefits of being a quasi if not real monopoly. On occasion, the competitive interests of the firm would suggest reasons to collaborate with their competitors as well as compete. They could combine to jointly activities such as research and development, or efforts to increase the social standing and appeal of their industry as a whole, or in joint political efforts to influence both government purchases and government regulation of their industry.
7. And, because the theory of industrial organization was concerned with sustained productivity gains, and that result was generated in large part by the rate at which innovations were created, tested, deployed, and diffused throughout the industry, the theory gave particularly close attention to the question of exactly where the innovations came from. This often focused their attention on how the research that could contribute to innovation at the basic or applied level was being produced: how much was there, who was producing it, and how was it being paid for. They also focused on the processes that moved from basic research to applied research to product and service development, to market testing, and diffusion.
8. As we have seen, there is every reason to suspect that these processes look quite different in the social sector in which the demand consists of consumer demand, voluntary contributions, and government spending, and the supply consists of commercial enterprises, nonprofit service delivery organizations, and government agencies.
9. Voluntary and government demanders/payers behave differently than individual consumers. They focus on wants and conditions they think are important and count as needs and rights rather than just consumer welfare. They focus on larger issues of equity as well as individual satisfaction, or the results achieved by a particular enterprise. They are often interested not only in advancing equity as a result, but also in acting equitably and fairly in the delivery of goods and services, and in efforts to create wider environmental conditions. Often, they make decisions as a collective rather than as individuals.
10. The nonprofit organizations and government agencies one can find on the supply side of social sector industries also behave differently than commercial suppliers. Nonprofit organizations and government agencies are loyal to missions that define value in terms of social results that includes but is not limited to client satisfaction. Both voluntary sector firms and government agencies are particularly vulnerable to and responsive to social pressure from social interests groups and the media precisely because they claim the role of acting for the public interest. Both voluntary sector firms and government are supposed to be open to and take advantage of their collaborative potential in achieving desired results rather than compete to be the enterprise that solved the problem. Voluntary sector firms and government agencies find it difficult to accurately measure the value they are producing, and that makes it difficult for those who are buying the social results the firms are producing to exercise the kind of accountability for performance that can reliably separate the good from the bad. In the place of performance accountability, both nonprofit and governance agencies are called to account for performance in terms of the reliability with which they follow “best practices” that are not really known to be best practices, and this kind of accountability tends to stifle innovation and obscure what constitutes performance rather than support it.[[3]](#footnote-3)
11. The mechanisms that support the activities that are particularly important to producing productivity gains – basic research, applied research, process and product research, production engineering, testing for value, launching as a sustainable enterprise, scaling up, -- are all also quite different in the social sector with the voluntary sector and government playing a much greater role.
12. So, we have a lot of work to do in trying to understand how the social sector really works to produce sustained productivity gains. And that knowledge is not likely to come simply by rehearsing Schumpeter’s theories for the commercial sector. To understand exactly how the various social sector industries work – the producing organizations that seek to move the needle on social conditions –it is critical to our ability to help social entrepreneurs figure out where to go with their creative energy, how to test the quality of their ideas, and how to get the good ideas into action frequently and quickly enough that we can observe the steady productivity gains in these industries that we are all hoping to see. We have long talked about the importance of understanding the ecology in which social enterprises work. And it may be that this metaphor and the methods associated with studying ecology will help us see the growth potential of individual social enterprises. But an alternative would be to adapt Schumpeter’s theory to the particular conditions of the social sector, and to learn more precisely and empirically about what can be done to improve the productivity of the particular industries that constitute the social sector through the use of the tools of industrial organization.

1. [↑](#footnote-ref-1)
2. Have also made progress in developing capacities to aggregate and direct voluntary constributions from small donors, but much of the attention has remained on the big foundations since they look the most like the powerful hedge funds. [↑](#footnote-ref-2)
3. Note that these problems do not come from the weakness of a particular institutional form, and would not be solved if all the nonprofit organizations and government agencies were commercialized. The come from the fact that these organizations are seeking to produce changes in social conditions whose value is both contested and hard to measure in the world they occupy. The same will be true for any organization entering these particular lists. [↑](#footnote-ref-3)