Social Entrepreneurship:
Mobilizing Resources for Success

By J. Gregory Dees

Say the word "entrepreneur," and most people quickly conjure up a vision of what that word means. For some, it might be the woman who starts a popular bookstore in a local mall. Others might picture someone who puts his life's saving (and perhaps a second mortgage on his home, and the outstanding balances of all his credit cards) at risk by buying a McDonald's franchise. Still others might imagine someone like Bill Gates, who with his partner Paul Allen founded Microsoft and built it into the world's largest software company, with annual sales topping $22 billion.

Although you may feel fairly certain that you know what entrepreneurship means in the world of business, you may be less clear about how the term applies to the world of nonprofits, where success is generally measured not by how much profit you make, but by how well you serve your social mission.

One important distinction is that social entrepreneurs do not receive the same kind of market feedback that business entrepreneurs get. Business enterprises that efficiently create value for their customers are rewarded in the long term—rewards that eventually find their way back to investors in the form of profits. Creating social value, in contrast, does not necessarily lead to long-term financial rewards for the enterprise or for the entrepreneur creating it. As a result, social entrepreneurs face different challenges, especially in attracting resources. They must be able to do more with less, and persuade others to provide resources on favorable terms.

When you think about resources for a social enterprise, fundraising is likely to be the first thing that comes to mind. If so, think again! Money is only a means to an end. It lies in the middle of a process that begins with your idea, as well as the intangible resources you bring to your venture, and ends with the capabilities you need to deliver your social results.

At its heart, entrepreneurship is about getting things done or changing the way things are done. It's not about amassing assets. Cash is simply a tool for helping you develop the capabilities you need in order to create the social value that lies at the heart of your mission.

Value-producing capabilities are a function of many factors. Skills, relationships, knowledge, integrity, and reputation are but a few of the intangible factors that are also needed for success. Money can help you attract people with skills, knowledge, relationships, and reputations, but it is not sufficient to ensure that they will employ their human capital effectively and creatively in pursuit of your mission. A shared commitment to your mission can be much more important than money in motivating your team to do what it takes to produce results.

Every social entrepreneur starts with a stock of intangible resources, including an idea, relevant knowledge, experience, relationships, reputation, passion, and commitment. These resources are used to attract the money and the other resources needed to get the venture off the ground. Savvy social entrepreneurs know how to convert their intangible resources into results, using as little money as necessary.

To assess your resource needs in a way that is truly entrepreneurial, you should

- Start with the result you want to produce, not the limited resources you have in hand.
- Consider less resource-intensive ways of achieving these results.
- Take into account the uncertainty that surrounds your venture.

Phase 1: Define the Capabilities Required for Success

Begin by conceptualizing your desired results and defining the capabilities needed to produce them. Based on your mission and the way you've defined your opportunity, you should have a specific idea of the way in which your venture will create its social value. This idea can be used to determine the things you'll need to do (or get others to do). Visualize your desired outcomes—the creation of value to your target audience—and then list all of the steps required to create this value, until you come to inputs that can be easily purchased on the open market.

For each step, describe the capabilities required to complete it successfully. Because most social ventures are service organizations, key steps are likely to include program or service development, marketing, service delivery, and follow-up or assessment. Each may involve different components. Once you've identified the key steps in your social value creation process, add the administrative capabilities that support this process.

Create the list of required capabilities for your new venture. Then challenge a knowledgeable friend, advisor, or teammate to find anything that might be missing from your list.

Phase 2: Devise a Resource-Smart Operating Structure

Now you can start to get creative. Building on your list of required capabilities, you need to devise a resource-smart operating structure, which is determined by your answers to the following questions:

1. *Which capabilities will you develop in your own organization?*
2. *Which capabilities will you get from suppliers or contractors?*
3. *Which capabilities will be delivered by partners?*

The first step is to imagine the range of possibilities. This can be done by going through the list of required capabilities and asking yourself: Could this capability be delivered by someone else? If so, who would that be and how would it work? Not all possible combinations are worth exploring, but it is helpful to consider seriously a few combinations that you didn't have in mind when you started. Many social entrepreneurs begin with a preconceived idea of how their organizations will work. This exercise may make you aware of new options.

Pick a Structure That Is Promising and Efficient

Now that you see the different roads, how do you decide which one to take? In advance of doing it, you may not know which structure would be optimal, but you can make a judgment call. Ask yourself these four questions:

1. Which capabilities are you particularly well suited to provide? Most social entrepreneurs bring distinctive capabilities to their ventures, things that they do particularly well. What strengths do you bring to this venture? Can you really do these things better than or more efficiently than others who are already out there? How do you know this? It makes sense for you to do the things you do best relative to other potential providers. If you are starting this venture with a partner, you can ask the same question of the partner.

2. Which capabilities are most crucial to the value-creation process? Some capabilities are likely to be more crucial than others; they have the potential for a disproportionate effect on the value created. To identify potential core capabilities, ask yourself: Is this an area in which errors are likely to be made without close attention to quality? If errors are made, how much damage will they do? You should be very cautious about contracting out any functions for which you are vulnerable to costly errors. What if you find that some functions are core to the venture, but you're not particularly good at them? You have two choices: (1) you can do what it takes to build the capability in-house, or (2) you can find a highly motivated and skilled partner to provide the needed capabilities. The latter option is likely to require fewer resources, but finding the right partner may prove to be difficult.

3. Which activities motivate and provide meaning for you and your team? If you or your initial team members particularly enjoy certain activities and do them reasonably well, you probably shouldn't outsource them—even if others could do them slightly more efficiently. Your venture isn't going to work for you unless you do at least some of the things you most enjoy doing.

4. Which capabilities can be bought more cheaply and easily than they can be built? Cost becomes important for capabilities that are not strengths, not crucial, and not passions of yours. Some capabilities can be built only through a major investment of time and money. Others are needed only on a temporary or part-time basis. In either case, it may be prudent to contract for the provision of these capabilities by others who have already made the investment. How easily could you build the needed capability? Do you know of outside providers who would provide it much cheaper than you could build it? If you cannot find outside providers at all, you may have no choice but to build the capability in-house.

Using these four questions, you can decide on an operating structure that builds on your strengths, protects core capabilities, keeps you motivated, and is cost effective. This should be a resource-smart structure. Of course, picking a structure is an art, not a science. You must make judgment calls based on limited information. As your venture unfolds and you learn more, your operating structure is likely to change. This process of considering other options should prepare you for change. For now, you simply need to define a starting point.

Phase 3: Develop a Resource-Smart Economic Model

With this operating structure in mind, you must develop an economic model for your venture that is also resource-smart. An economic model describes where funds will come from and where they will go in your venture. It addresses two key questions: (1) Will you generate operating revenues to reduce your need for outside resources? and (2) On what terms will you acquire the various inputs for your venture?

Your economic model is likely to change over time as you get a better sense of what's feasible. For now, make judgment calls and be creative. The Social Enterprise Spectrum on this page can help.

You should think of this spectrum as describing a continuous range of choices with purely philanthropic and purely commercial options as the extreme endpoints. Your venture is likely to be somewhere in the middle, but where? Consider each stakeholder dimension—beneficiaries, capital providers, workforce, and suppliers.

Beneficiaries: Capturing Some of the Value You Create

You can reduce your need for outside resources by finding a viable revenue stream that does not hamper your ability to serve your mission. You need to ask the following questions:

1. Who benefits (or could benefit) from your venture?
2. Is it appropriate and practical to charge them a fee for this benefit?
3. How much could you charge while still achieving your social objectives?

You should consider three possible sources: your primary intended beneficiaries, third parties with a vested interest, and parties who benefit indirectly from your activities.

Many social entrepreneurs are reluctant to charge their primary beneficiaries, especially when the beneficiaries are poor or are seen as deserving the benefit. This reluctance is morally appropriate in some cases, but it can also be patronizing. Sometimes charging a fee, even a small one, can add to people's sense of empowerment and responsibility. Charging fees screens out those who aren't serious. Those who choose to pay a fee tend to have a greater commitment.

Moreover, charging a fee opens you to a market discipline that can be helpful. If no one will pay, you may not be delivering the value you think you are. Paying also gives beneficiaries more right to complain than if they receive free services. Creative structures can be developed to address affordability issues. These structures include sliding scales (with lower fees for poorer people), scholarships, and deferred payment options.

Could you get contracts with third parties who have a vested interest in your success? Two likely candidates are the government and business owners. Government agencies may save money by contracting with you for service delivery to those receiving government benefits. Employers may provide access to social services to improve employee productivity. In either case, you may be able to contract for service provision. Of course, third-party payment doesn't have all the advantages of user fees because the party most directly benefiting isn't making the payment decision. This can be dealt with by using a hybrid system, with intended beneficiaries making small co-payments.

Can you find ways to charge people who benefit indirectly from your success? Many social entrepreneurs are finding ways to create enterprises that serve their mission and generate revenue from customers who are not the primary beneficiary. Think of a restaurant that serves as a job training program for homeless youth, or an eco-tourism venture that educates participants about environmental issues and uses profits to support conservation activities. By producing private benefits for paying customers, you may also be able to serve your social mission. It is worth considering ways to align the interests of paying customers with programs that create social value.

Capital Providers: Raising Cash from the Right Sources

Even if you can charge fees, you are likely to need startup capital, working capital, and expansion capital. Social ventures that don't generate sufficient earned income to cover all operating costs also need to raise ongoing operating subsidies. You need to ask the following questions:

1. From whom could you raise capital for your venture?
2. What are all the costs associated with these capital sources?
3. Which are likely to be the most cost-effective sources for serving your mission?

What are your options? If you are planning to set up a nonprofit venture, you could get capital in the form of (1) grants and donations, (2) recoverable grants (similar to zero-interest loans in that you have to repay all or part of the grant), (3) below-market-rate loans, (4) tax-exempt market-rate loans or bonds, (5) full-market-rate loans, and (6) above-market-rate loans (made by loan sharks).

These options are arranged according to repayment costs. If you create a true for-profit business to serve your mission, you can also tap into equity funding.

Equity investment has very different characteristics from debt. Equity holders take more risk in that they get paid last, after all debt obligations are covered. Equity has no fixed repayment schedule but has an unlimited upside. Debt holders get no more than the interest they were promised. Equity holders make their money from profit distributions and by selling their interest, either back to the organization or to someone else. If you plan to use equity capital, consider what kind of return your equity holders will expect and when. It's important to have an exit plan for them.

Could you repay capital providers? If you do not plan to have any sources of earned income, it will be hard to attract providers who are looking for a return. In theory, you could repay investors out of future grants and donations, but few investors will bet on your will and ability to do that. Besides, your future donors may well object to their money being used to pay off earlier investors.

Why not just use grants and donations for everything? Grants and donations may seem like the resource-smart way to raise capital, even if you expect to have strong earned-income streams. In many cases, they are the best source for startup and early-stage capital, but not always. For one thing, grants and donations are not free. Even though you do not have to repay them, grants impose costs. In evaluating your options, you should consider all of the acquisition costs (including the time it takes to get approval), the costs of managing and maintaining the relationship (including meeting restrictions and special reporting requirements), as well as the costs of depending on a funding source that may not be easily renewable.

Other sources may prove to be more cost-effective, more responsive to the timing of your needs, less restrictive, and more renewable. Reducing dependence on philanthropic funds can also be symbolically important for organizations that want to signal their commitment to self-sufficiency. Finally, if you can repay capital providers, it frees up those funds for investment in other projects, including your future projects. It is a form of recycling cash, which is resource-smart in a global sense. By not tying resources up in a venture that can repay them, they are freed for use in ventures that truly need them.

When should you consider repaying capital providers? Even for new social ventures with earned-income potential, it can be hard to raise capital that must be repaid. Without a track record of producing income, most lenders or investors will not be sufficiently confident in your will and ability to repay. Even for-profit social-purpose businesses are often perceived as risky investments. Either you will need to find investors looking primarily for a social return or you will need to demonstrate a strong potential upside for them.

Workforce: Balancing Compensation and Performance

The single most important factor in your success is your team. Their skills, attitudes, and other intangible assets can make all the difference when it comes to your success. Your economic model has to make some assumptions about whether and how much you will pay for the human capital behind your organization's capabilities. Ask the following questions:

1. What skills are needed to support your in-house capabilities?
2. Which, if any, of these skills could be effectively supplied by volunteers?
3. Should a commitment to volunteerism be part of your mission?
4. How many and what kinds of paid staff will you need?
5. How well will you pay them?

There is a wide range of workforce strategies in the social sector. Some organizations rely heavily and successfully on part-time volunteers, including in major leadership positions. Other organizations put a premium on professionals and use volunteers only in limited roles—as board members, fundraisers, and advisors. It is worth thinking through different possibilities for staffing your venture.

What should be the role of volunteers? The answer to this question should be driven by practical considerations and values. On the practical side, you have to ask which functions could be legitimately, effectively, and reliably provided by volunteers. This will vary widely from venture to venture. Using volunteers is clearly the low-cost way to deliver your services, where it is feasible. Even so, it may not be the resource-smart approach if it does not produce desired results.

For some organizations, the use of volunteers is a core value and part of the mission. It allows them to create an additional kind of social value—the value that arises from private citizens joining together voluntarily to provide for the common good. If this is part of your mission, then it should be included in the outcomes you intend to produce and given appropriate weight in your staffing decisions. It may compensate for some inefficiencies.

How well should you pay your staff? Few organizations can function effectively without at least some paid staff. Where you don't use volunteers, you must decide on compensation levels. How easy is it to get this skill at below-market wages? Is a low wage sustainable? Although low wages are common in the social sector, this practice may not be resource-smart if it makes recruiting difficult, increases turnover, or contributes to low morale. People in the social sector often accept lower wages because they care about the cause. In effect, they're donating their foregone wages to the venture for a "social return." Low wages help ensure that you are getting people who care about your mission and not just the money; however, even with this kind of commitment, it can be demoralizing when your staff members have peers in the business world who are making orders of magnitude more. You want to find a wage level that is optimal for producing results by attracting and retaining productive and committed team members in key positions.

Suppliers: Efficient Deals, Sustainable Relationships

In finalizing your economic model, consider your suppliers, including any contractors or partners needed to deliver required capabilities. To define your economic model, you need to ask the following questions:

1. Of the capabilities others will provide or support, which are most crucial?
2. What is the best way to ensure that crucial capabilities will be provided reliably?
3. What is the most cost-effective way of ensuring that non-crucial capabilities are supplied with adequate quality and reliability?

As with other stakeholder relationships, many different arrangements are available, including in-kind donations, discounts, and market-rate contracts.

How do you build strong relationships with suppliers, contractors, and partners? In selecting an operating structure, you have already identified crucial capabilities. You should revisit that list with particular attention to those crucial capabilities that you plan to leave to others. These are your most crucial suppliers, contractors, or partners. It is particularly important that you structure your relationships with them so as to ensure high-quality, reliable performance. These suppliers, contractors, or partners should highly value their relationship with your organization for business reasons, social reasons, or, ideally, both.

Business reasons can be either direct or indirect. The most direct business reason is that you are a major paying customer that supplier would not want to lose. This kind of power will be out of reach for many new social ventures in their early stages. Indirect business reasons include the close relationships

you may have with important customers. Perhaps your board chairperson provides a great deal of business to this supplier. Indirect business reasons are more common and can lead to in-kind donations, pro bono services, or significant discounts.
The main social reason to value a relationship with you is a shared commitment to your social mission or at least to an integral part of it. Social reasons can also lead to favorable terms; however, if this is the primary source of strength in your relationship, you need to make sure the supplier's commitment is enduring and deeply held.

What kinds of financial terms are appropriate for partners? If the capability is crucial and the supplier is deeply committed to the same values as you, it might be resource-smart to create a partnership. You could co-sponsor programs, with both of you putting your reputations at stake. The economic implications of a partnership vary depending on its terms. The flow of funds is a strategic choice determined by the relative strengths and weaknesses of you and your partner. Which of you is best positioned to provide funding and which one has the strongest bargaining position?

Consider different economic models: Based on your preferred operating structure, define two or three distinct, but plausible economic models for implementing that structure. These models should differ significantly on at least two dimensions of the Social Enterprise Spectrum. Which one do you think will better serve your mission while making effective and efficient use of scarce resources?

How to Reduce Your Initial Cash Needs

Here are 10 tips that could help reduce your cash needs in the early startup stage. This isn't about thinking small or handicapping yourself by starting with too few resources. It's about doing more with less cash. You have to assess whether any of these tips are useful to you based on their effect on your ability to serve your mission. If a specific tip would jeopardize your mission, don't do it!

Tip 1: Stage your venture, funding only one or two stages at a time.

Staging investments is a powerful tool for resource management. The idea is to raise just enough cash to reach your next major milestone, or just beyond it. Once you reach the first milestone, you should have more information to use in raising additional funds. Although this technique is common in the venture capital world, it is not so common with foundations. If you wait until you've demonstrated results from the first stage of your venture to write a proposal for the second stage, it could be months before you get your next grant. The delay could be deadly. You may need to educate your foundation partners in order to get them to see the value of proceeding in stages, putting more funds in as you both learn more.

Tip 2: Convert fixed costs into variable costs.

Fixed costs are the costs you incur no matter how many people you serve or projects you complete, such as rent, utilities, compensation for full-time salaried employees, and so on. Variable costs go up or down based on your level of activity. You can convert fixed costs into variable costs by changing the way you pay. Royalties, commissions, piece-rates, and the like make the costs variable. For example, if a school pays all its teachers a salary, teaching becomes a relatively fixed cost. This could be converted to a variable cost by paying teachers on a per-student basis. Payments often have both fixed and variable components. The idea here is to incur costs only when you are delivering your service. This is particularly helpful for earned-income ventures because their revenues are tied to service delivery, but it can be useful in other ventures as well. Lower fixed costs usually mean lower startup costs and lower operating costs in the first few months of operation, as you build up your volume of activity. Your cash needs go up only if you are successful, in which case you should be in a stronger position to raise more money.

Tip 3: Look for excess capacity and underutilized resources.

Identify potential suppliers that have recently expanded their facilities or lost a big customer. For example, businesses that move into new offices often have more space than they need right away, leaving room for growth. If you're willing to start off with temporary office space, they might be willing to give you a deal. In terms of human resources, people who are unemployed are more motivated than people with jobs. If you need help with accounting, recently retired CPAs may welcome the chance to put their skills to work for you.

Tip 4: Help new suppliers establish themselves.

Businesses, law firms, and accounting firms that are new to your area will be aggressively looking for business. They may be willing to strike a good deal to get the work and build their reputation. On a personal level, newcomers to a community may be looking for ways to get involved. Newly promoted executives or professionals may be looking for ways to gain experience and visibility in community leadership. Of course, you take more risks with new players, but you'll generally get a better deal. You have to make a judgment about how much risk you can take in a particular area.

Tip 5: Make yourself a low-cost customer.

Make an effort to understand your resource suppliers' economics. You may see ways to reduce their costs of serving you. Many businesses experience times when they are busy (peak) and times when things are slack (off-peak) during a day, a week, or even a year. If what you need could be provided during off-peak times, the supplier should be motivated to give you a better deal.

Tip 6: Make yourself a value-added customer.

You may be able to find ways to provide additional value to your suppliers beyond what you might pay. Your status as a social entrepreneur gives you special leverage with potential for-profit resource providers. Helping you may enhance their reputation, if you give them public recognition. You may have other supporters who would be inclined to give their business to this supplier, if the supplier offers you a favorable deal. This could be formalized as a "cause marketing" campaign in which your relationship is used to generate business for the supplier.

Tip 7: Explore the possibilities of sharing assets with others.

Many of the resources you need could be shared with others. Think of copiers, fax machines, conference rooms, even someone to answer the phones. Of course, you have to deal with the logistics and structure a fair arrangement, but if you can make this work, it can lower your cash needs significantly. This is one of the benefits of business incubators, where young businesses share all kinds of resources. Nonprofit incubators are not as common, but they do exist. Often the incubator offers technical assistance, as well as sharing of facility costs with other new ventures. Incubators aren't intended to be permanent homes. You need a plan for weaning yourself from the incubator's assistance that fits with the incubator's policies regarding when you should exit.

Tip 8: Make sure the cash you have on hand is working for you.

Manage the cash you do have carefully, by collecting early, paying only when payments are due, and earning interest on your balances. Any excess above your immediate needs should be earning interest. You don't want to tie money up for long periods, but it should be invested in a way that will make it available when you need it. This is particularly important for managing large grants that come in at the beginning of the grant period. You can maximize the cash invested by managing your cash flow wisely. This means collecting cash as early as possible. You should politely make sure you are paid in a timely fashion. Conversely, don't pay your bills any earlier than necessary. This keeps your cash in the bank. There are at least two exceptions to this rule. Some suppliers will offer you a discount to pay early. If you're earning only low interest rates on your cash, it may be worth it to avail yourself of the discount. The second exception is more strategic. If this is a particularly important supplier with which you want to build a strong and long-term relationship, you may want to pay earlier. If you have the cash, the forgone interest may be worth giving up to strengthen the relationship.

Tip 9: Take advantage of special deals and shop for bargains.

If you shop around, you can often find resources that will serve your purposes adequately, but that aren't first-rate or are offered under special terms and conditions. The Internet is making the search for deals even easier. Consider buying used furniture and equipment. It's often easy to get used furniture and equipment donated as an in-kind gift. Contact colleges or universities in your area to find out if they have courses that require students to complete research or community service projects, or if they run supervised internship programs. Look for group rates. Insurance and employee benefits are two areas in which associations often get better deals than individual organizations could get on their own. You may have to join an association to get the deals, but it could be worth the cost. Finally, take full advantage of your nonprofit status to get access to free goods, special prices, pro bono services, and volunteers.

Tip 10: Negotiate on price, but only with those who can cut a deal.

Everything is negotiable, but front-line customer service representatives rarely have the authority to go beyond standard discounts. Few of them would reap any benefits from cutting a special deal. If you want to press further, go up the chain of command until you reach someone who would reap the benefits and has the authority. If it's a small business, go to the owner. If it's a chain or larger business, find someone with "profit-and-loss" responsibility. For example, in a law firm or accounting firm, this would be a partner.

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