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The Role and Sustainability of Social Enterprises in the Hungarian Economy

The economies of the Central and Eastern European countries have suffered a significant decline as a result of the geopolitical changes of 1989-90. A number of enterprises with low efficiency, obsolete technology and product structure closed down. The lack of new productive capacity led to a sharp rise in unemployment. The recession, inflation and employment problems particularly affected Hungary's regions. A series of social enterprises have been set up to improve employment in disadvantaged municipalities, as a result of local and government initiatives. In their study, the authors review their spatial distribution, their impact on the local economy and society, and the challenges related to the sustainability of their operations.

Keywords: social innovation, disparity, sustainability, Entrepreneurship

JEL-CODE: O35, Q56, L31, M14

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Introduction

The output of the economies of Central and Eastern European countries, the competitiveness of products and services declined significantly as a result of the geopolitical changes that took place in 1989-1990. A series of companies with low efficiency, outdated technology and product structure have closed. Due to the lack of new production capacities, unemployment has skyrocketed. Recession, inflation and employment problems did not affect regions Hungary same extent. In the former so-called heavy industrial areas, a number of mines and metallurgical plants have closed. As a result, unemployment in these cases was higher than the national average.

In order to improve employment in disadvantaged areas and settlements, local and government initiatives have led to the establishment of a series of social enterprises since the early 2000s. However, some of them became inoperable after the end of the subsidy period and were liquidated. In their study, the authors analyse the territorial distribution of social enterprises in Hungary, the reasons for their choice of location, their impact on the local economy and society, and the challenges related to the sustainability of their operations. Our aggregate sustainability index, calculated on the basis of our questionnaire survey, confirms that the sustainability of enterprises consciously generating social innovations and striving for renewal is better than that of enterprises lacking innovation.

Hungary economic, employment and demographic structure has changed as a result of geopolitical changes after 1989. The loss of Eastern European markets has exposed shortcomings in the international competitiveness of domestic products. The decline in economic output has affected different regions of the country differently. In the eastern part of the country, where heavy industry (mining and metallurgy) used to dominate, the crisis was more severe, while the western part of the country was able to regenerate faster with the appearance of foreign capital.

As a result, a vicious circle of the economy developed in the eastern part of the country: the shrinking employment capacity of traditional manufacturing industry meant that the low-skilled became unemployed and then long-term unemployed. At the same time, the number of people living below the poverty line increased, private consumption fell, which had a negative impact on production, etc. Nearly 60% of the higher-skilled workforce left these regions in search of a better living.

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Literature background of the topic, research questions

The concept and idea of social (social) innovation and entrepreneurship appeared in the literature in the second half of the 1980s. The aim is to bring disadvantaged groups back into the world of work and to provide them with income through new and novel, i.e. innovative solutions.

There are many definitions of social innovation in the literature. *Kocziszky et al.* (2017) define social innovation as a concept that aims to help groups lagging behind, in difficulty, and to develop and apply new and novel employment solutions, structures and incentives.

According to *Ziegler* (2017) "Social innovation is the implementation of new combinations of capabilities" (p. 256).

According to *Howaldt and Schwarz* (2010, 2016), social innovation is a new combination of social action. Innovation is therefore social in the sense that it is socially accepted. This definition is also used by *Agostini et al.* (2019) and *Kaletka et al.* (2012).

According to the *Stanford Center for Social Innovation* (2009), it is a new solution to a social problem. This definition is also used by *Prasad and Manimala* (2018) and *Svensson and Bengtsson* (2010).

According to *Phills, Deiglmeier, and Miller* (2008), it is a novel solution to a social problem that is more efficient and sustainable than existing solutions, and the value created affects society as a whole, not individuals. This definition is also used by *Prasad and Manimala* (2018) and *Scaffidi* (2019).

Moulaert, MacCallum, Medmood, and Hamdouch (2013): considers practices related to certain forms of social justice and the transformation of existing power relations as social innovation. This definition is also used by *Pradel-Miquel* (2017).

According to *Neumeier* (2016), social innovation is a change in the attitude, behavior or perception of a group of people through the interconnection of a network of coordinated interests that, relative to the horizon of the group's experience, lead to new and improved ways of collaborative action within and beyond the group. This definition is used by *Soma et al.* (2018).

According to *Mulgan, Tucker, Ali, and Sanders* (2007), social innovation is a set of innovative activities and services that are motivated by the satisfaction of social needs and are predominantly developed and disseminated by organizations whose primary goals are social in nature. This definition is also used by *Prasad and Manima* (2018).

European Commission (2010): Social innovation is a new idea that seeks to urgently address unmet needs. Innovations that are social in both their ends and means. Social innovations are new ideas (products, services and models) that simultaneously meet societal needs (more effectively than alternatives) and create new social relationships or collaborations. This definition is used by *Heinze and Naegele* (2012).

Nelson and Sampat (2001): includes social technologies such as forms of division of labor and modes of coordination.

Our literature analyses clearly confirm that since the early 2000s there has been a sharp increase in the number of studies dealing with social innovation, including its economic issues. (Figure 1)

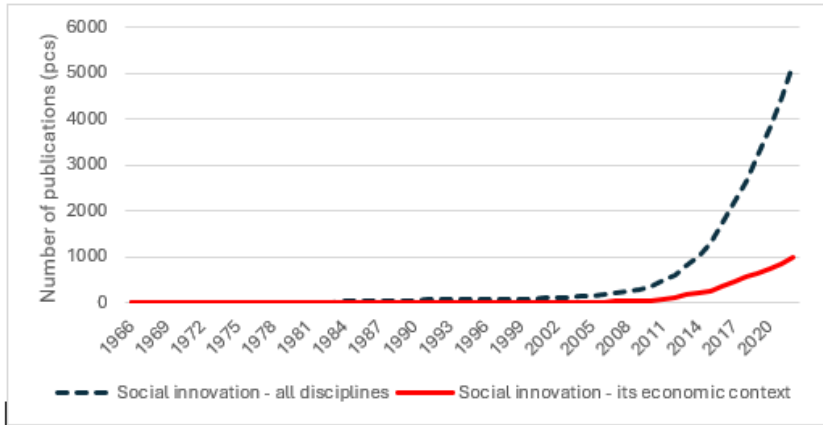


Figure 1: Development of the number of relevant publications (1966-2022) - (pcs)

Source: own editing

Most of these studies mention problems (poverty, lack of economic sustainability, unemployment, ageing, infrastructure deficiencies, environmental sustainability problems, etc.) that the authors seek to solve with the help of social innovations. (Figure 2)

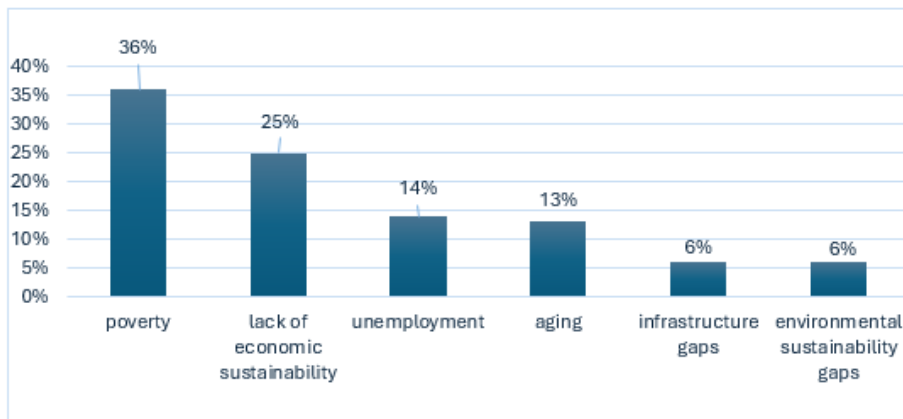


Figure 2: Distribution of social problems outlined in studies in 2022 (%)

Source: own editing

About 40% of the studies are theoretical, where the authors propose new frameworks and models for studying social innovation; barely thirty percent discuss solutions (e.g. Heinze & Naegele, 2012). Most studies use qualitative methods or focus on a single case (e.g. Agostini et al., 2019). The authors rely on in-depth interviews and secondary data (reports, websites, databases, archives, etc.) for their empirical analyses.

A similarly colourful picture is encountered by anyone who wants to get a comprehensive picture of definitions related to social enterprises. We understand that the purpose of social entrepreneurship is complex: it integrates business and social expectations, unlike private sector organisations, which are normally motivated by business goals.

It follows from the above definition that social enterprises essentially seek to solve problems at local level. The scope of most of them is therefore local. Those who see social enterprises as an engine of social change must be right (Crowther et al., 2022 and 2024).

Foundations and mutual insurance funds can be considered as the forerunners of social enterprises (Defoumy et al., 2009; G. Fekete & Lipták, 2011). The attention of those working on the subject, as evidenced by the increasing number of publications, has increased since the 1990s.

At the same time, the profile of social enterprises has become increasingly complex over the last three decades, as local communities increasingly recognise the need to solve problems locally. On the other hand, there is a growing need to strengthen entrepreneurship.

In the course of our research, we seek answers to three questions:

- 1) What is the role and weight of social enterprises in the Hungarian economy?
- 2) What justifies assessing the sustainability of social enterprises?
- 3) What are the conditions for the sustainability of social enterprises and how can they be ensured?

The structure of our study follows the answers to the above questions.

The relevance of social innovations and entrepreneurship in the Hungarian economy

After 1989, fundamental social and economic changes started in the Central and Eastern European region, including Hungary. As a result, the competitiveness of domestic products has decreased. The loss of previous markets has created a vicious circle in the economy, which has led to increased unemployment, a fall in private consumption and an increase in the number of people living below the poverty line. (Figure 3)

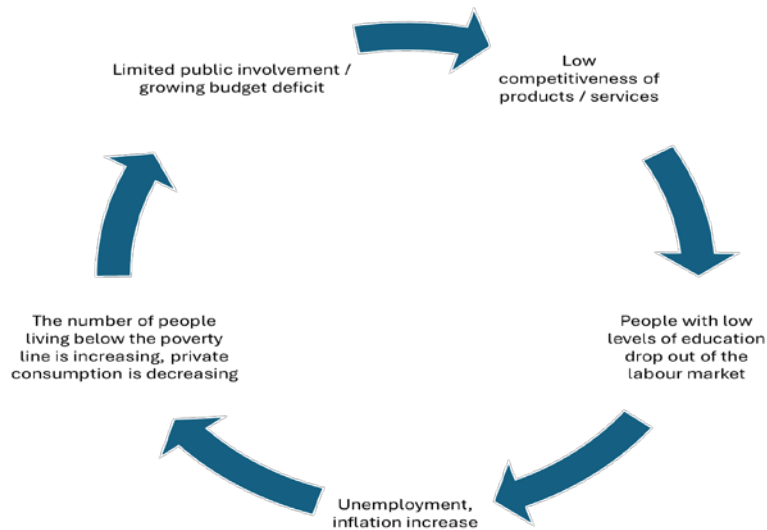


Figure 3: Logic of negative changes in the Hungarian economy after 1989

Source: own editing

Between 1989 and 1993, gross domestic product fell by 18% in Hungary and the number of people employed decreased by 15%.

This process lasted until the end of the 1990s. Subsequently, economic expansion began to grow spectacularly, which was broken by the 2008 financial crisis. (Figure 4)

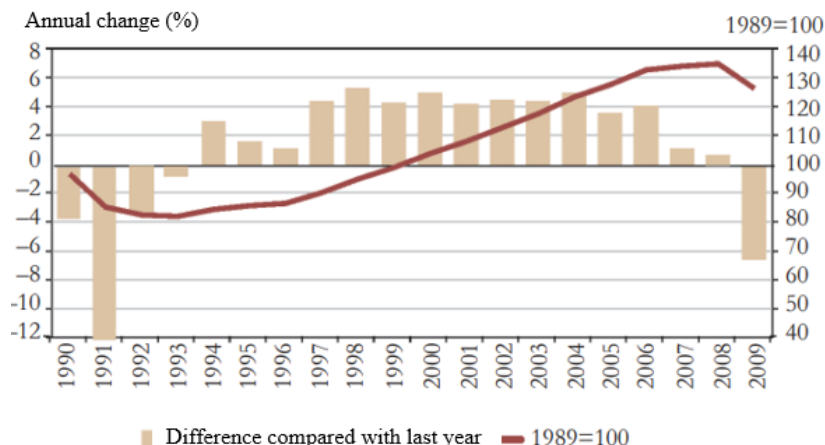


Figure 4: Development of the volume of gross domestic product in Hungary (1990-2009)
Source: KSH, 2010. p. 30.

With the economic downturn and rising unemployment, the number of people receiving social assistance has increased. (Figure 5)

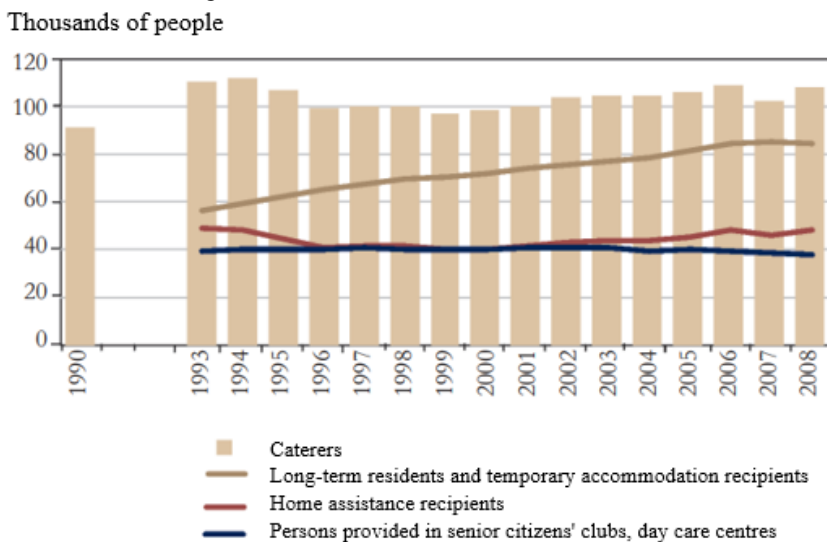


Figure 5: Number of persons receiving social assistance (1990-2008)
Source: KSH, 2010. p. 21.

Due to the income situation, the deterioration of employment, the increase in unemployment, the former regions of heavy industry (mining, metallurgy) were particularly affected. As a result, significant territorial disparities have developed in the country, which the state budget could only undertake to a limited extent due to lack of resources.

Employment and existential tensions had an adverse effect on demographic and social processes. The number of live births decreased, the dependency ratio increased, and the activity rate deteriorated. The risk of children growing up in families with low-level unemployment benefits finding it more difficult to integrate into the labour market has increased, in the absence of positive examples.

As a result of mostly government (top-down) initiatives, social innovations have gained in value and the first social enterprises have been established, especially in disadvantaged, crisis-stricken regions with a lower human development index. (Figure 6)

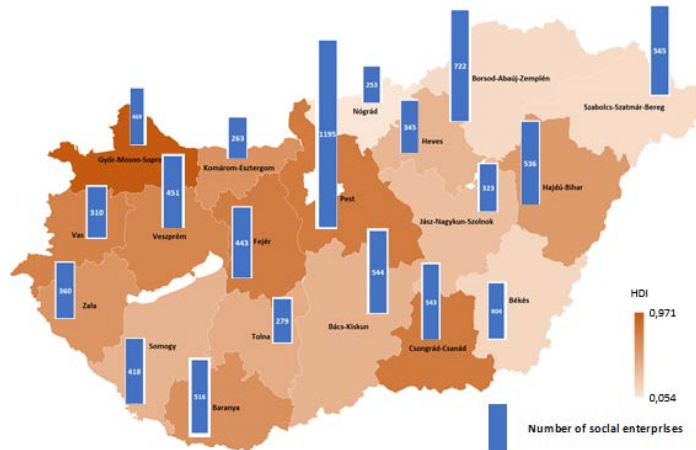


Figure 6: Number of HDI and social enterprises in Hungary (2022)

Source: own editing

There are three relatively distinct phases of social entrepreneurship in Hungarian practice. Top-down period (basically 2000-2010). In the first period, society received this form of enterprise, which was mostly supported by government initiative and resources, with reservations. Due to the lack of social acceptance and prepared management, most of these startups turned out to be short-lived (Harangozó, 2022). An important result of the period was the detection of the fundamental problems that society expected answers from these enterprises (Table 1).

Table 1: Problems that social enterprises can address

Social problems	Economic problems	Ecological problems
<ul style="list-style-type: none"> - high rates of female unemployment, - underemployment of low-skilled people, - long-term unemployment of disadvantaged people, <ul style="list-style-type: none"> - extreme poverty, - exclusion, - family breakdown, - permanent disengagement from the world of work. 	<ul style="list-style-type: none"> - low local supply and demand, - the exodus of more skilled workers, - impoverishment, - economic infrastructure. 	<ul style="list-style-type: none"> - locally generated waste, - ecological degradation of the living environment, <ul style="list-style-type: none"> - lack of regenerativa resources, - land depletion, - reduction of green spaces, - increase in environmental damage.

Source: own editing

Period of emergence of demand for social innovations (2010-2020). It was then that it became clear that social enterprises could not be operated permanently without local initiatives, innovations and innovators. An increasing number of social enterprises have partnered with universities, research and consulting organisations to generate innovations.

Table 2: Typical social innovations

Social area	Economic area	Ecological area
<ul style="list-style-type: none"> - cultural heritage management, - educational support programmes, - public catering programs, - active care programs for the elderly, - Dementia prevention programs, - self-confidence building programs, - sensitization in relation to persons with disabilities, - development of narrative skills. 	<ul style="list-style-type: none"> - social market, - social employment, - development of local brands, - organization of farmers' days, - generating start-ups / smart programs. 	<ul style="list-style-type: none"> - waste recycling, - ecological routes, ecological school operation, - generation of conscious ecological lifestyle programs, - operation of an ecological forum.

Source: own editing

A key feature of the third period is the focus on operational sustainability (from 2020). At the beginning of the decade, the recognition that sustainability is a fundamental criterion for running social enterprises was reinforced. In connection with this, more and more attention has been paid to quality employment, supporting social mobility, improving well-being, making better use of capacities and building network connections.

Rationale and model for sustainability proofing of social enterprises

The first social enterprises appeared in Hungary at the end of the 1990s as one of the options for dealing with cumulative ecological, social and economic problems. However, these organizations proved to be short-lived after the end of government subsidies (Harangozó, 2022).

There were several reasons for this, including: lack of acceptance of bottom-up initiative, lack of management preparation, lack of ideas to support the continued operation of organizations, unfounded business plans, high turnover and lack of prior (ex-post) sustainability assessment of ideas. For more than five years, therefore, our attention has turned to examining the sustainability of social enterprises.

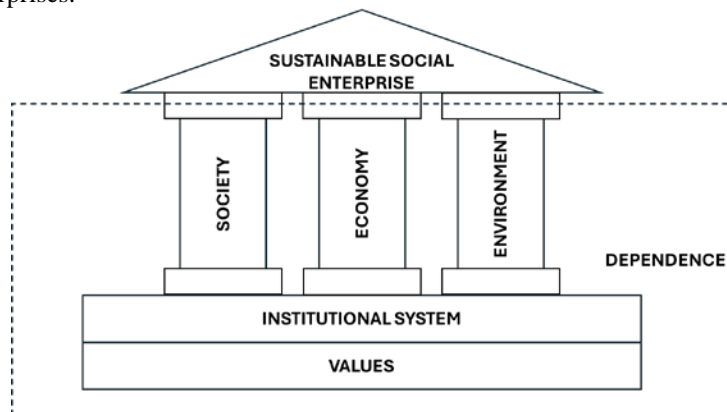


Figure 7: Pillars of sustainable social enterprise

Source: own editing

Sustainability traditionally looks at environmental, ecological sustainability. Social enterprises, on the other hand, require a complex, institutional, social, economic and ecological approach. (Figure 7)

The basis of sustainability is the value system of the given community, which allows or hinders the creation, help and support of community enterprises. It acknowledges or protests against the state using part of its tax to help disadvantaged groups and regions catch up.

Such elements of the value system that support the establishment and operation of social enterprises:

- respect for resources,
- social sensitivity,
- spatial justice,
- transparency,
- individual and community responsibility,
- diligence,
- respect for laws and regulations,
- respect for built and intangible heritage.

The objectives of social enterprises differ from those of private enterprises. Priority is given to improving local employment, securing income and reducing the number of people receiving benefits.

The legal and regulatory background supporting the establishment of social enterprises, civil and/or governmental organizations play a decisive role in the value system. The value system shapes the institutional system in a good or debatable direction. Values and institutions can provide the social, economic and environmental pillars of social enterprise sustainability.

In other words, the state of values, institutions, society, economy and environment are closely dependent and causal.

With this in mind, the sustainability process of social enterprises can be developed (Figure 8).

The formulation of goals starts with a governmental (top-down) or local (bottom-up) initiative. The result of the development of new or novel ideas is the project, which should be an ex-ante sustainability assessment as an integral part of its feasibility assessment. Based on the project's outputs, an ex-post examination of municipal/territorial impacts and operational sustainability of the enterprise can be carried out.

Monitoring sustainability is not a one-off task, but a permanent one, and its results have a fundamental impact on the lifespan of social enterprises.

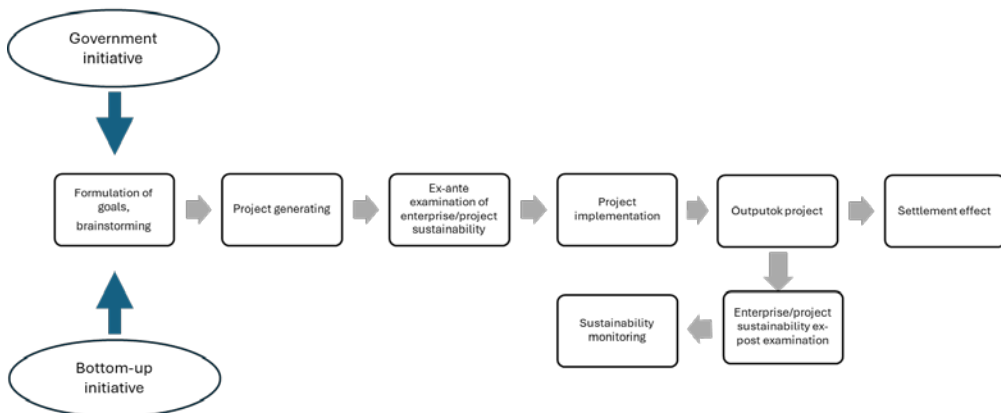


Figure 8: Place of sustainability proofing in the operational process of social enterprises

Source: own editing

Analysis of sustainability is a permanent task and part of the microprudential toolbox. Reaching the built-in critical indicator levels (institutional, economic, social, ecological) of a well-structured monitoring system draws attention to the need for intervention.

The lifespan curve of a social enterprise consists of the same phases (foundation, growth, fulfillment, aging, decline) as that of organizations belonging to the private sector. However, there is an interesting difference in the duration of each phase. According to our studies, nearly two-thirds of social enterprises go bankrupt or close to liquidation after 2.5-3.5 years after foundation.

Model output indicators and definition of the aggregate sustainability index

The sustainability assessment is based on economic, social and environmental output indicators. (Table 3)

When defining the indicators, we aimed for simplicity and easy quantification. Economic sustainability was examined using 12 indicators, social sustainability with 6 indicators and environmental sustainability with 6 indicators.

The indicators express a percentage change, which facilitates comparability over time and across organizations. Based on the indicators, six sub-indicators (employment, management, income, network, emissions and circular economy) were formed.

Table 3: Model sustainability indicators

Name of partial index	Name of subindex	Name of sustainability indicator
Economic sustainability (GRI)	<i>employment status of entrepreneurship</i> RÉ(1)	a1 - change in the number of employees (%)
		a2 - unemployment rate in employment (%)
		a3 - share of early school leavers in employment (%)
		a4 - change in female employment rate (%)
		a5 - change in staff turnover (%)
	<i>economic status of entrepreneurship</i> RÉ(2)	b1 - change in net sales turnover (%)
		b2 - change in value added (%)
		b3 - change in balance sheet profit (%)
		b4 - change in subscribed capital (%)
		b5 - change in liabilities (%)
		b6 - change in cash flow ratio (%)
		b7 - change in labour productivity (%)
Social sustainability (TRI)	<i>workers' income situation</i> RÉ(3)	c1 - change in wage level (%)
		c2 - share of women in business management (%)
		c3 - change in dependency ratio (%)
	<i>social relations</i> RÉ(4)	c4 - change in female-male earnings gap (%)
		c5 - change in non-profit relationships (%)
		c6 - change in for-profit organizational relationships (%)
Environmental sustainability (KRI)	<i>emission effects</i> RÉ(5)	d1 - change in greenhouse gases (CO2 equivalent) (%)
		d2 - change in the amount of solid waste emitted (%)
		d3 - change in public water consumption per employee (%)
	<i>circular economy</i> RÉ(6)	d4 - share of renewable energy sources in total energy consumption (%)
		d5 - circular material use rate (%)
		d6 - share of area under organic farming (%)

Source: own editing

The Aggregate Sustainability Index (AFI) was determined in three steps (Figure 9):

1. In the first step, six sub-indices were formed based on the percentages of sustainability indicators by simple arithmetic averaging.
2. In a second step, economic (GRI), social (TRI) and environmental sustainability (KRI) partial indices were defined.
3. In the third step, we determined the Aggregate Sustainability Index by multiplying the three partial indices as follows:

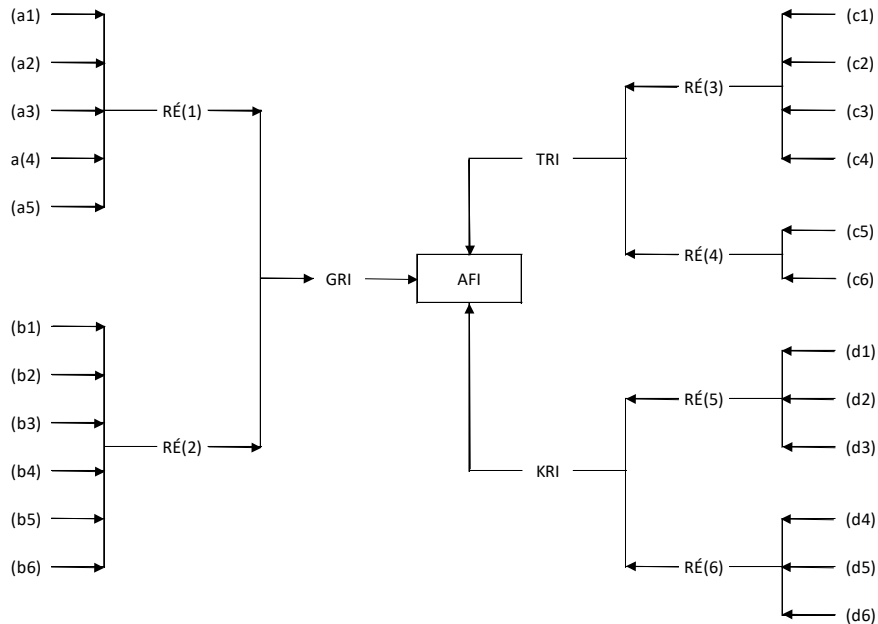


Figure 9: Logic of creating an Aggregate Sustainability Index

Source: own editing

The individual indicators and sub-indices draw attention to the weak points of the organization and the decisions that can be made based on them.

Ultimately, an aggregate index expresses the sustainability of a social enterprise in the form of a single number between zero and hundred.

For each partial and sub-index, risk levels have been determined on the basis of experience as follows:

- 0 - 30% – danger zone;
- 31 - 40% – high risk;
- 41 - 60% – medium risk;
- Above 61% – low risk.

Results of empirical studies

Our questionnaire and interview survey to examine sustainability indicators was first conducted in 2019 and then in 2023. We assessed responses from 132 organisations to ensure comparability over time.

Profile of organisations

The organisations covered by the study are mainly active in agriculture (37%), social welfare (25%), waste processing (12%) and woodworking (6%). Organizations classified in other categories (26 years) have the longest history, but associations (20 years) and foundations (16 years) are also above average. The youngest are social cooperatives (7 years) with a low employability (5 people). The largest employers are foundations (27 people) and other non-profit organizations (25 people).

Management of organisations

94% of respondent organisations are still operating; 2.3% are newly formed organizations and 3.7% are currently non-operating organisations. 12% of organisms are in the start-up phase of the life curve, most (47%) are in the growth phase, 36% are in the maturity phase, and 5% are in decline. More than half of the surveyed companies rely on tender funds not only to start their activities, but also to maintain their continuous operation. 30% of respondents answered that they did not rely on tender funds at all at the start.

The largest proportion (36%) of revenue in 2021 was income from basic and public benefit activities, central state support (22%), tender support (19%), income from business-type activities (10%), municipal support (8%), other subsidies (6%).

58% of the organisations surveyed reinvested their profit after tax into their social activities.

Staff conditions of organisations

A significant majority of female employees are present in the organizations surveyed (63%). In terms of age group, most employed people (60%) are aged 25-49, nearly a quarter are aged 50-64, 10% are aged 16-24, and only 3% are over 65.

Most work full-time (79%). The share of part-time employees is 2%. The vast majority of employees (65%) are employed. The frequency of all atypical forms of employment (agency contracts, public works, voluntary work, simplified employment, member employment relationships) is below 10%.

The majority of organisations (86%) employ people with full capacity. 46% employ workers who are disadvantaged in the labour market.

Sustainability of organisations

Our calculations confirmed that the sustainability of the organizations examined is scattered. The differences in employment, emissions ($\Delta=34$) and farming ($\Delta=30$) are particularly great, depending on the population of the settlement, the profile of the enterprise and its situation within the country.

The smallest difference was found in circular economy sustainability (Figure 10).

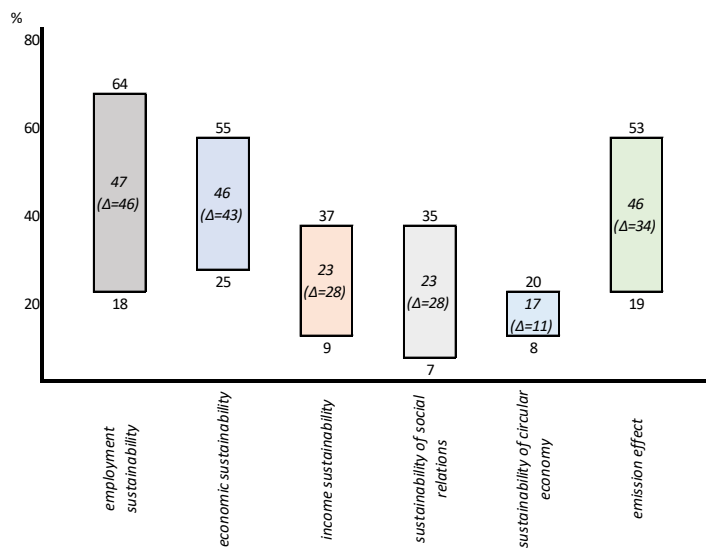


Figure 10: Minimum, maximum values and average of sustainability sub-indices

Source: own editing

The calculations confirmed that 53 of the 132 organizations examined had an aggregate index of high risk, while 72 companies had an index classified as medium risk. Only 7 entrepreneurship (5 %) had low sustainability risks (Figure 11).

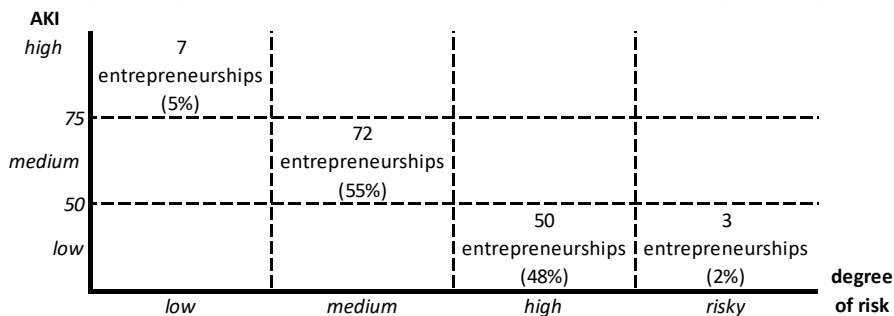


Figure 11: Risk matrix of the 132 social enterprises examined by the aggregate sustainability index

Source: own editing

This risk measure is also expressed when summarizing data from individual organisations (Table 4).

Table 4: Sustainability indices (%) of the 132 social enterprises examined

Partial index		Sub-index		Aggregate index value
name	value	name	value	
employment	47	economic sustainability	47	32
economic status	46			
income status	27	social sustainability	25	
social relations	23			
emission effects	46	environmental sustainability	28	
circular economy	17			

Source: own editing

Between 2020 and 2023, 37 (47%) of businesses with low and medium sustainability risk (79 in total) consciously sought to innovately renew their operation, profile, marketing and image: they are open to their environment.

Final thoughts

The geopolitical shift and the transition to a market economy caught both theorists and practitioners in countries belonging to the former Eastern European bloc unprepared. This has had and continues to have serious social and economic effects over several years.

It is no coincidence that in the case of so-called transition economies, including Hungary, the role and importance of social enterprises has increased, especially in the case of disadvantaged regions and social groups. One of the priorities of the European Union's planning periods 2014-2020 and 2021-2027 is to give special support to the development and implementation of social innovations. Our research shows that the importance of social enterprises will continue to grow in the future. Therefore, it does matter how stable their operation is.

More than 60% of Hungarian social enterprises were established between 2010 and 2020 through top-down initiatives. Of these, nearly 42% will have to limit their operations within two years of the end of support. This creates tensions at both macroeconomic and municipal levels.

Since the early 2020s, there has been a substantial change. During their operation, more and more enterprises consciously engaged in generating innovations (relying on their own resources or involving external experts). As confirmed by our primary and secondary data collection, this

significantly contributed to the economic, ecological and social sustainability of the social enterprises surveyed.

Ex-post and ex-ante examination and monitoring of sustainability can contribute to the stable and predictable operation of social enterprises.

The model presented in our study and its sub- and aggregate indices, which can be calibrated between zero and one hundred based on the model, are intended to help this "good-host" type of thinking.

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