

# Perceived Opportunities by Social Enterprises and their Effects on Innovation

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## SUMMARY

*Social enterprises can play an important role in reducing inequality within a society and can also contribute to long-term economic development. Using a database based on the responses of 220 Hungarian social enterprises we first identify the business opportunities that they perceive. We conclude that social enterprises operating in different legal forms have different perceptions of their opportunities, and we speculate that this has an effect on their innovation activity as well. It is striking that – with the exception of social cooperatives – none of the Hungarian social enterprises see current or future social and/or market needs and demand as a major opportunity. This suggests that only social cooperatives have the incentive to focus their innovation efforts on social and market needs. Almost all social enterprises, on the other hand, have high expectation for European Union funds; the threat is that social innovation is driven by the targets set by the authorities allocating European funds, instead of the needs of the society.*

*Keywords: business opportunities, inequality, social enterprises, social innovation*

*Journal of Economic Literature (JEL) codes: B55, L31, O35*

*DOI: <http://dx.doi.org/10.18096/TMP.2019.02.01>*

## INTRODUCTION

The most influential theoretical works published in the field of economic theory in the last two decades have all emphasised that the unprecedented growth in wellbeing in the West can be attributed to such related factors as the equality of citizens as regards to their rights, obligations and opportunities, political pluralism, and inclusive economic institutions (North et al. 2008; Acemoglu & Robinson 2012; McCloskey 2016). It has also been observed in the last decades that income and wealth inequality has been on the rise in developed nations (Piketty 2014), while median income has been dropping, or stagnating at best (Brynjolfsson & McAfee 2014). Calculations made by Nolan et al. (2018) show that there is an increasing gap between real GDP per capita and average household median income in many Western countries, including Hungary. In the period 1979–2014 the real GDP per capita increased by 80% in the USA, while median household income only grew by 15%. According to official statistics, Hungarian real GDP per capita had grown at a mere 1% in this period, while according to Nolan et al.'s calculations the median household income growth rate was over 2% less than that, so it actually decreased in this period (Nolan et al. 2018).

The increasing income gap threatens to destroy the equality of opportunity (the foundation stone of the Western societies), and so it threatens long-term growth prospects as well. One of the main goals of social innovation is to decrease income inequality. But, as stated above, equality is one of the keys to economic growth, so social innovation can also generate long term growth. As social innovation is primarily carried out by social enterprises, in this study we focus on them and on their perceived opportunities. Social innovation can also contribute to goals related to sustainable development, another issue that is regarded as crucial by many (Kis-Orloczki 2019).

The first section of this study gives an overview on the general connection between social innovation and social entrepreneurship. In the second section the data and methods are introduced, while the third section presents an analysis of the perceived opportunities of social enterprises. The study ends with a short conclusion section.

## LITERATURE REVIEW ON SOCIAL INNOVATION AND SOCIAL ENTREPRENEURSHIP

The literature on social innovation and social entrepreneurship is very diverse. An OECD report compiled in 2010 lists nine definitions for social innovation (OECD, 2010, pp. 214-215), and twenty-nine for social entrepreneurship. Some of the definitions are very simple, which gives room to various interpretations; some others are extremely complex. According to Mulgan, social innovation is a group of new and working ideas that target social needs that were not satisfied before (Mulgan et al. 2007).

The more complex definitions typically also stress the collective nature of social innovation (Lazányi 2017). Westley and Antadze define social innovation as “the complex process of introducing new products, processes or programmes that profoundly change the basic routines, resource and authority flows, or beliefs of the social system in which the innovation occurs” (Westley & Antadze 2010, p. 2). When comparing it to traditional, Schumpeterian innovation, the LEED programme of OECD defines social innovation as a process that “is not about introducing new types of production or exploiting new markets in itself but is about satisfying new needs not provided by the market (even if markets intervene later) or creating new, more satisfactory ways of insertion in terms of giving people a place and a role in production” (cited by Nicholls et al. 2015, p. 3). After reviewing a number of options, Nicholls et al. finally settle on the following definition: “varying levels of deliberative novelty that bring about change and that aim to address suboptimal issues in the production, availability, and consumption of public goods defined as that which is broadly of societal benefit within a particular normative and culturally contingent context” (Nicholls et al. 2015, p. 6).

Before settling for a definition, we set out the framework of our analysis. According to the Acemoglu-Johnson-Robinson (AJR) model (Acemoglu et al. 2004), the innovative effect of market competition and the horizontal relationships during competition can be sustained if the political system creates rules that strengthen them. The political system, on the other hand, is only likely to create such rules if it is pluralistic. These conditions create the best environment for long-term growth; however, there are further frictions, such as the various types of market failures and the income inequality rising from market competition. Such failures lead to the rise of government intervention. Government intervention has its well-known failures, too: disregarding the preferences of politically less active groups, low efficiency, and subpar decisions due to information asymmetries and collective action problems. As a result of these deficiencies the government can also fail in the

reduction of inequality, and so the equity of opportunities, the basis of long-term growth cannot be sustained.

The primary benefit of social innovation is in its role in preventing social and economic seclusion. Although social innovation is often not measured in monetary terms (because social benefits in the form of intangible assets are a lot more important), it requires the investment and continuous use of material resources, and so the traditional business sustainability conditions apply to it as well. In other words, the selective process of market competition applies to social innovation (unlike in the case of government-run projects). We believe that social innovation should be defined in a way that excludes the government sector, and as a process that is primarily regulated by market competition. In this interpretation social innovation is a product, service, process or resource allocation method that is introduced to take care of partially or completely new market needs, its main goal is to achieve social benefits, and it is controlled by the selective forces of market competition.

Social innovation projects may be undertaken by many different agents. For-profit businesses are often involved in such projects; corporate social responsibility has given rise to many such examples in recent years. The government may also undertake social innovation projects (through government-owned enterprises, for example). However, the ultimate goal of for-profit businesses is profit maximisation; for the government it is vote maximisation, so we are safe in assuming that the majority of ideas producing social benefits would come from other agents. These other agents are similar to traditional businesses, on the one hand, because they need to raise their own revenues for their operation. But they are also similar to the government on the other hand, because they aim to achieve social benefits. These agents defined by a double bottom line will be called social enterprises in this study.

How can an idea that aims to achieve social benefits be financially sustainable if it has to compete with ideas that were either selected to generate profits (and so should be more efficient from a financial point of view), or are financed from tax revenues (so are not under revenue-generating pressure)? A theoretical answer can be easily phrased by relying on the fundamentals set forward in this study, but the practical answer can be more problematic. The following possibilities can be mentioned:

1. The social enterprise operates in a market where transaction costs are so high that the traditional business model is not efficient (e.g. cooperatives).
2. It offers ideas and products that are highly valued by the community, and so consumers are willing to pay a higher price than the market average (e.g. organic products, locally produced goods, handcraft goods).
3. They are small and so they can better focus on the real needs of the community, and the incentives to make a meaningful effort are much stronger than in large government-run projects.

4. They are entitled to a government subsidy that is paid according to some performance indicator (e.g. charter schools).

Social enterprises are the main initiators of social innovation projects. They compete with either business entities or government agencies for survival. Their operation is based on real needs of the community, and their successful operation is highly influenced by the institutional environment. The rules of the game and the legal form of their operation are important factors in the operation of social enterprises. Innovations generated by these firms also depend on factors the managers believe are the most important for the future development of their firms. The second part of the study focuses on these issues by investigating the perceived opportunities of the social enterprises.

## DATA AND METHODS

The data for this study come from a survey that was conducted by the Faculty of Economics, University of Miskolc in 2017 by a team lead by Éva G. Fekete and Ágnes Horváth Kádárné. The survey was sponsored by the Hungarian Employment Agency OFA, within the project called PiacTárs – Priority project for the support of social enterprises, and for the creation of a sustainable and competitive social economy. A total of 220 social enterprises were surveyed, 46 of which were non-profit limited liability companies (NLtd), 57 associations (Assn), 39 foundations (Fdn), and 59 social cooperatives (SC).

The objective of this study is to identify the business opportunities offered by the environment as perceived by

the managers of social enterprises and to detect the differences among them according to their legal form. A partial SWOT analysis was conducted in order to detect the special characteristics of the different legal forms. The survey offered 15 possible factors that can create business opportunities, and managers were asked to pick the ones they felt were the most significant for their organisations. During the analysis we ranked these factors according to the number of mentions in our sample, and we also calculated the rank for the four different legal forms. To make the rankings easier to read, in this study we only discuss those factors that achieved at least 10% of mentions, so at least 10% of the respondents picked them as a significant opportunity for their organisations.

## RESULTS AND DISCUSSION

When broken down according to legal form, the factors mentioned in Table 1 are those that managers perceive as the most important opportunities for their organisations. There are two columns for each type of social enterprise. The first column shows the rank of that given factor according to the number of mentions (e.g. the third most frequent opportunity selected by the managers of social cooperatives was the “More EU funds” option); the second number shows the share of respondents who chose that given factor (e.g. 13% of the SC managers selected “More EU funds” as a significant opportunity for their organisation). The final column of Table 1 (Dif.) shows the rank gap of the given factor among the different legal types (e.g. the highest rank of “More EU funds” is 3<sup>rd</sup>, the lowest is 14<sup>th</sup>, so the Dif. column has a value of 13-4=9).

Table 1  
Most important perceived opportunities for Hungarian social enterprises (n=220)

Factor	SC		NLtd		Assn		Fdn		Dif.
More EU funds	<b>3rd</b>	<b>13%</b>	<b>3.</b>	<b>17%</b>	14.	1%	3.	9%	9
More private funds from individuals	14th	1%	11th	3%	<b>2nd</b>	<b>14%</b>	10th	5%	12
Better image of the sector in the society	9th	4%	<b>2nd</b>	<b>20%</b>	5th	7%	5th	8%	7
Better opinion on the sector by politicians	11th	3%	<b>4th</b>	<b>16%</b>	6th	7%	5th	8%	7
Higher market demand for the products/services	<b>2nd</b>	<b>16%</b>	13th	1%	<b>4th</b>	<b>10%</b>	6th	7%	11
Higher social need for the products/services	<b>1st</b>	<b>26%</b>	8th	3%	13th	1%	<b>1st</b>	<b>17%</b>	12
Improvements in economic environment of the country/region/settlement	4th	8%	<b>1st</b>	<b>21%</b>	<b>1st</b>	<b>14%</b>	8th	6%	7
More willingness for volunteer work	5th	7%	6th	6%	<b>3rd</b>	<b>10%</b>	<b>2nd</b>	<b>13%</b>	4

SC = Social Cooperative; NLtd = Non-profit limited liability company; Assn = Association; Fdn = Foundation.

Source: own calculations based on G. Fekete et al.'s survey (2017)

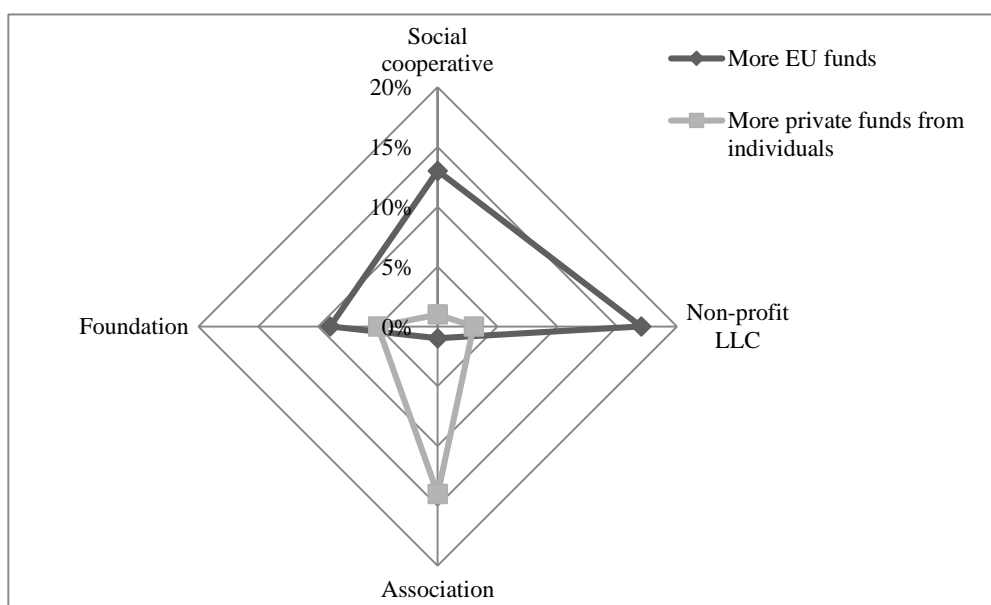
Table 1 is not the easiest to review, but it still gives a good idea about the most important perceived opportunities, and it also shows quite clearly that there are considerable differences among social enterprises with different legal forms (see the “Dif.” column of Table 1). Figures 1 to 4 give a clearer picture of these differences.

Figure 1 compares two possible opportunities (“More EU funds” and “More private funds from individuals”) among the four types of social enterprises. NLtds and SCs perceive the “More EU funds” option as one of the most important opportunities; for Fdns it is still ranked high, but it only has a 9% share, while it is only ranked 14 (out of 15) among Assns, with only 1% of the respondents picking this option. Those organisations which do not see the EU funds as an opportunity have to rely on private funds. Figure 1 gives a very clear picture of this substitution effect.

Other responses gained from this survey show that NLtds and SCs are by far the most business oriented in

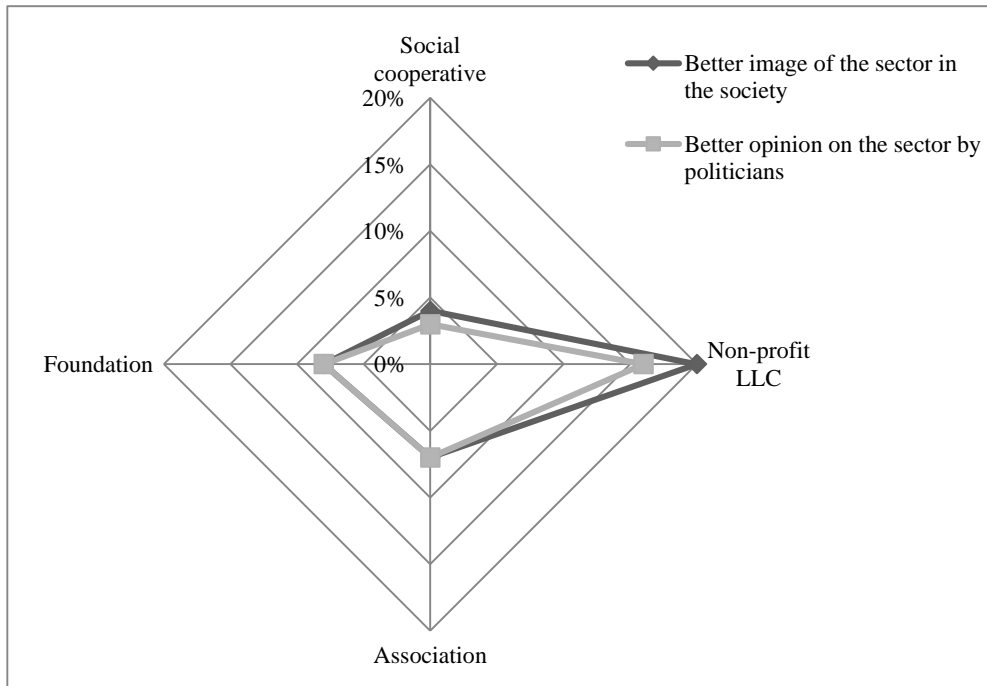
nature (meaning that they are the ones that rely on market revenues the most). Figure 1 also makes it clear that even these business oriented organisations want to rely on EU funds, and so are likely to focus on the preferences of the fund allocation authorities.

Figure 2 presents the evaluation of two factors that typically are fairly strongly correlated: the current image and future changes in the image of the non-profit sector in the society in general, and among politicians, or the political scene in particular. The two factors received similar mentions within all subcategories of social enterprises, but there are differences among the different legal forms. NLtds especially regard these two options as a significant opportunity, while the other legal forms, and particularly the SCs, are sceptical about them. This is especially bad news for Fdns and Assns, since according to the textbook business models these organisations should rely on a mix of private and public funds the most.



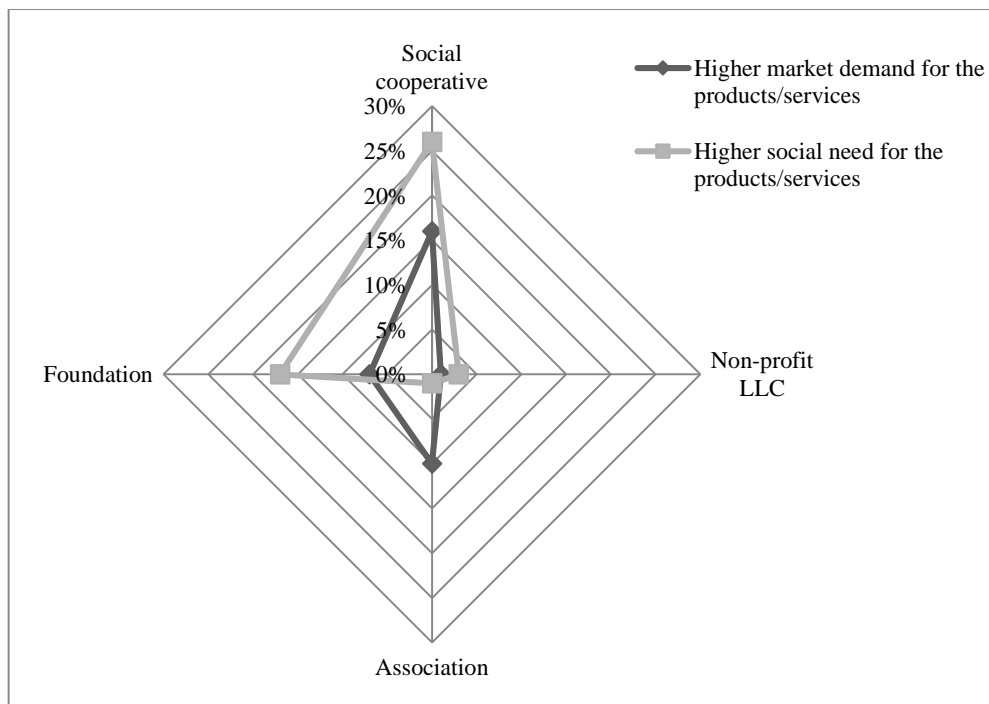
Source: own calculations based on G. Fekete et al.'s survey (2017)

*Figure 1. Share of mentions of “More EU funds” and “More private funds from individuals” as an opportunity, by the four legal forms of social enterprises*



Source: own calculations based on G. Fekete et al.'s survey (2017)

Figure 2. Share of mentions of “Better image of the sector in the society” and “Better opinion on the sector by politicians” as an opportunity by to the four legal forms of social enterprises

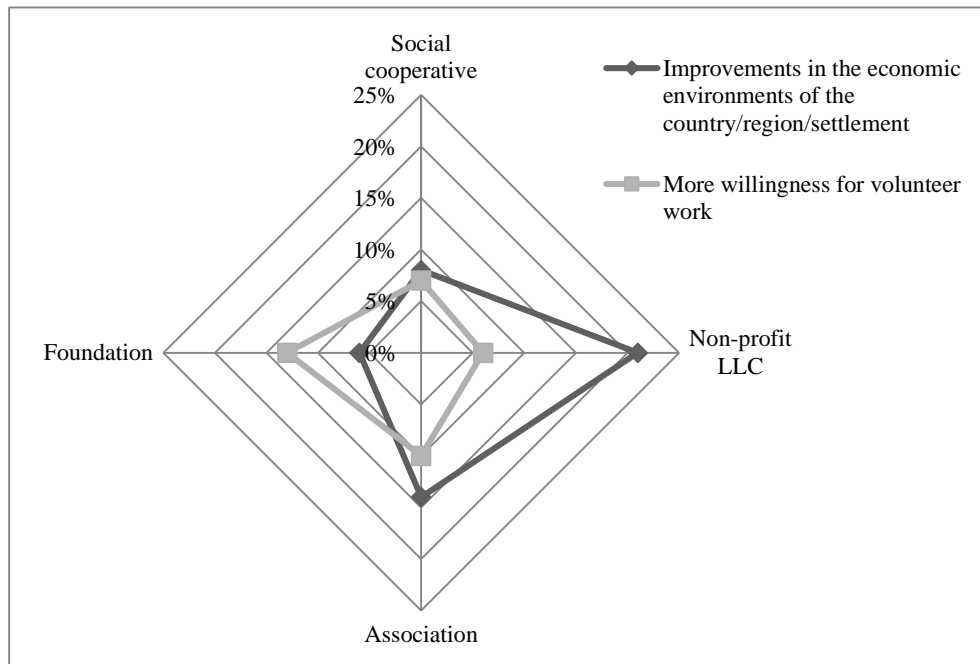


Source: own calculations based on G. Fekete et al.'s survey (2017)

Figure 3. Share of mentions of “Higher market demand for the products/services” and “Higher social need for the products/services” as an opportunity, by the four legal forms of social enterprises

As shown by Figure 3, the majority of social enterprises are sceptical about the possibility of a positive change in the market demand or in the social need for the products and services offered by them. Again, significant

differences exist in their perception according to the legal form of operation. The contrast is most striking in the case of market demand, and between NLtds and SCs. As already mentioned, these two types of enterprises rely the



Source: own calculations based on G. Fekete et al.'s survey (2017)

Figure 4. Share of mentions of “Improvements in the economic environments of the country/region/settlement” and “More willingness for volunteer work” as an opportunity, by the four legal forms of social enterprises

most on market revenues, and this makes the contrast even more alarming. By comparing Figures 1, 2 & 3, we can conclude that the managers of NLtds and SCs perceive their opportunities in a completely different way. NLtds aim to rely on EU funds, and public funding in general, and are sceptical about their market expansion opportunities. This approach can make them more focused on the agenda of the government and less focused on social and market needs when articulating their innovation plans. SCs, on the other hand, are optimistic about the possibility of a market expansion and are more sceptical about receiving more public funds. This may be reflected in their innovation objectives as well, which makes them the subcategory within social enterprises that is most suited to the role of generating long-term growth through social innovations that reduce inequality within the society.

The two factors included in Figure 4 are not as closely related to each other as the previous ones. The better economic environment is most strongly seen as an opportunity by NLtds, while volunteer work is a focus of Fdns and Assns. It is according to expectations that more business oriented enterprises (SCs and NLtds) would rely less on volunteer work, but this should be reflected in innovation goals as well. Firms that want to rely more on volunteer work have to be more sensitive to social needs. As far as the economic environment is concerned, again many social enterprises (but SCs and Fdns in particular) do not get their hopes high, and do not expect that they could profit from an improvement in the economic conditions. This makes them more reliant on public funds.

## CONCLUSION

The role of social enterprises is crucial in an environment where the growth rate of the typical (median) income falls behind the rate of economic growth (or in extreme cases median income even decreases). The widening median income – real GDP gap decreases the opportunities of many citizens and slows down the long-term growth rate. Social innovations carried out by social enterprises can reduce both market and government failures and can offer better solutions to social challenges, and so they can contribute to a fairer society that gives more equal opportunities to its citizens.

Social enterprises may fulfil this key role only if there is no considerable difference between the theoretical model presented in this study and the actual perception of managers about their role and opportunities in the society. In this study we have pointed out some warning signs. The majority of the social enterprises surveyed in 2017 do not see the increase in market demand and social needs as a realistic opportunity in the near future. If market and social needs do not represent a significant opportunity for them, this may be reflected in their innovation projects, too, more precisely in the lack of social/market focus of these projects. There are exceptions, though, especially the social cooperatives, which are closest to our theoretical model in this sense.

If the needs of the market or the society are not in the focus of the innovation strategy of these social enterprises, other factors determine the priorities. Social enterprises may turn towards stakeholders that could provide a safer and more predictable access to resources. Volunteers, public organisations, and EU organisations are such possible stakeholders. Only associations expect considerable help coming from private sources (and foundations have positive expectations about volunteer work). Foundations, social cooperatives and non-profit limited liability companies see public funds, especially EU funds, as a safer and more promising option. Non-profit Ltds are optimistic about internal public funds, too (since

they see the better opinion on the sector by politicians as a significant opportunity).

These results suggest that the primary task in most of the social enterprises is not to sell their social innovation ideas to the market or to the society but rather to the government (be it at the national or the European level). To be more precise, the managers of the majority of the surveyed social enterprises see a much bigger opportunity in receiving public funds for their social innovation projects than in relying on market demand. We have also shown that the reliance on public funds is increased by the fact that many social enterprises do not expect to profit from an improvement in the economic conditions of their immediate or wider environment.

#### Acknowledgement

*This research was supported by the project no. EFOP-3.6.2-16-2017-00007, titled Aspects on the development of intelligent, sustainable and inclusive society: social, technological, innovation networks in employment and digital economy. The project has been supported by the European Union, co-financed by the European Social Fund and the budget of Hungary.*

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