

Scaling the impact of the social enterprise sector

October 2016



Authored by:

Arjan Keizer
Audrey Stickers
Hagar Heijmans
Robert Carsouw
Wouter van Aanholt

Contents

1. Introduction: Social enterprises come of age	3
2. The rise of the Dutch social enterprise sector	5
3. Impact and financial performance of social enterprises	11
4. Vision for the social enterprise sector	20
5. Challenges for professionalization and further growth	22
6. Opportunities and recommendations for sector growth	24
Acknowledgments	26

1. Introduction: Social enterprises come of age

In 2011, McKinsey published ‘Opportunities for the Dutch Social Enterprise Sector’, its first report on social enterprises in the Netherlands. The sector was then in an early stage of development – if you could speak of a sector at all. Social enterprises have multiplied since then, and their societal impact has grown. The sector is now well recognized and attracts more attention from public, investors and beneficiaries. Its supporting infrastructure has strengthened significantly with more direct interaction with municipalities, education institutions and corporates on their CSR initiatives. This report provides an overview of developments in and around the sector, its state today, and recommendations to strengthen and expand the sector’s impact in the years ahead.

How we now define social enterprises

In ‘A map of social enterprises and their eco-systems in Europe’ the European Commission defined a social enterprise as ‘an operator in the social economy whose main objective is to have a social impact rather than make a profit for its owners or shareholders’. In this report, we refer to organizations that aim to make more than 50% of their revenues from commercial activities.

We exclude those owned by traditional commercial companies and public organizations. We do not set limits on profit distribution, nor do we explicitly apply the EU governance criteria, because while transparency, fairness and balanced roles are important, they are hard to measure objectively.

Although we chose this definition simply to set the scope for deeper analysis, it is different from the one we used in 2011. It widens the definition from companies making more than 75% of their revenue from commercial activities, more in line with other European countries. On the other hand, it excludes organizations with a social mission, such as ASN Bank and Greenchoice, because they are part of larger commercial entities.

Using this approach has a material impact on the number of social enterprises in the Netherlands, and on how we calculate their size and financial performance.

It’s difficult to overstate the sector’s importance to communities, institutions and industries. As people’s social needs grow and municipalities and government agencies struggle to marshal the financial and human resources required to meet those needs, social enterprises are bringing entrepreneurs, communities and capital together in new ways. Together, they are addressing seemingly intractable problems with solutions that have mostly eluded governments and for-profit businesses, inspiring citizens to contribute and spurring investors and leaders across industries to experiment and think more broadly about the meaning of success.

Our research shows that social enterprises are now playing a larger role than ever in the Netherlands, and that they have large opportunities to grow in size and positive influence on society.

Many organizations aim to have a positive social impact, from public sector organizations to traditional businesses that use some of their profits to serve the common good,

as shown in Exhibit 1. The trend we're discussing here, however, is the rise of enterprises whose main objective is to have a social impact rather than make profits for their owners. Putting social impact first is what identifies social enterprises as an emerging and independent sector.


Exhibit 1: **Types of organizations and their aims**

Social Value				Financial Value			
Public organizations & NGO's		Social Enterprises				Traditional business	
Grants only	Grants and market income	Potentially sustainable >50% trading revenue	Breakeven all income from trading	Profit surplus reinvested	Profit distributing social driven	Impact important, not first	CSR company Mainstream commercial company

Traditional businesses increasingly prioritize social impact, driven by stricter reporting guidelines, their own ambitions, and their need to attract talented people who place more weight on the social impact of their career choices. Many of these businesses are doing more to increase their corporate social responsibility. Some traditional businesses move towards being social enterprises, Gulpener being one example.

Gulpener

This brewery, established 1825, produces beer in a socially responsible manner. Procurement is local and organic, and production is close to CO₂-neutral. The family business began moving towards social entrepreneurship in 2001 by signing the 'Verbond met de Natuur', an extensive ambition statement to do business in socially responsible and sustainable ways.



© www.gulpener.nl

While we recognize that the social impact is achieved more broadly, this report focuses on social enterprises as an emerging and growing sector with distinct characteristics, target audiences, financing and business models. Although ideas, enterprises and their impact are created by people, it is the enterprise that, as a type of organization, has its own place in the economy.

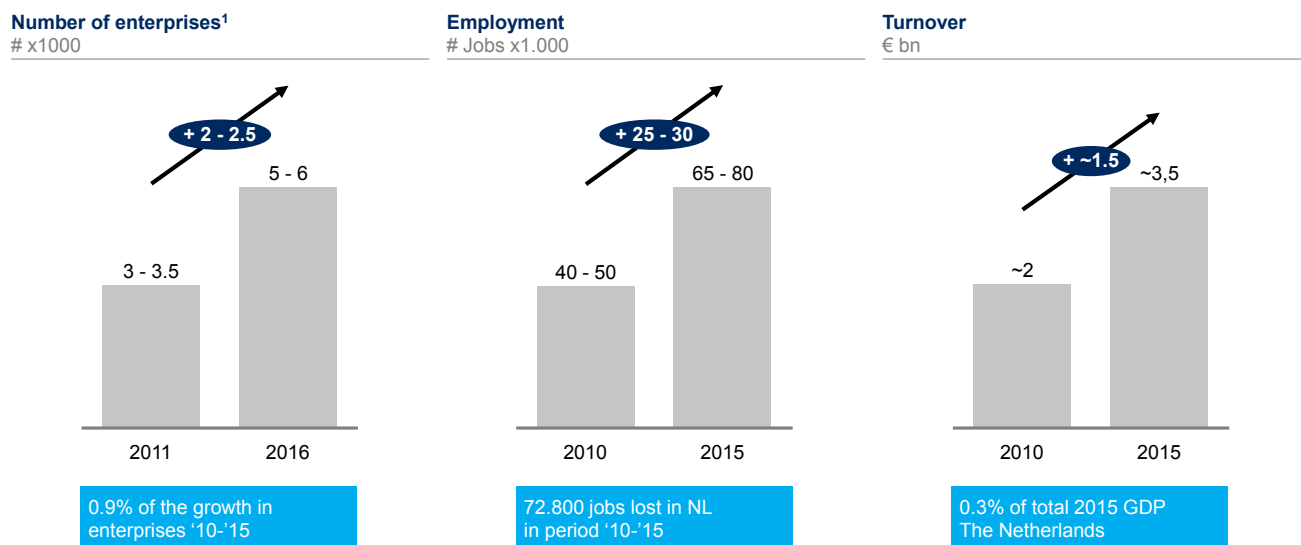
Based on a survey of 182 social enterprises, interviews with 25 sector experts, social entrepreneurs, investors and public sector representatives, and a large body of literature on the topic, this report provides an overview of the state of the Dutch social enterprise sector and its trends and developments. It offers insights into challenges and success factors, and it offers recommendations to further unlock its growth potential.

2. The rise of the Dutch social enterprise sector

Employment and revenues nearly doubled along with the number of social enterprises

Over the last five years, the social enterprise sector in the Netherlands grew by 2,000-2,500 enterprises to 5,000-6,000, expanding the sector by about 70% and representing ~1% of the total increase in the number of all companies since 2010 (Exhibit 2).¹

Exhibit 2: The growth of Dutch social enterprises



¹ Number of enterprises was 4,000-5,000 in 2011 rapport. Difference due to better data availability and application of 2013 EU definition

SOURCE: Statistics Netherlands (CBS), Chamber of Commerce, McKinsey Social Enterprise survey (N=182)

Since 2010, jobs in the social enterprise sector have increased by more than 60% to 65,000-80,000 in 2016. These 25,000 new jobs came at a time when the Netherlands lost nearly 75,000 jobs in other sectors. Total revenues in the social enterprise sector rose from about 2 billion in 2010 to 3.5 billion euros in 2015, an increase of 75%.

About 3,000 new enterprises started since 2011, generating a year-on-year growth of 20%. In the next five years, we expect additional growth from traditional businesses who change their missions towards 'impact first' and thereby meet the definition of a social enterprise, likely starting with family businesses and followed by small and medium-sized enterprises (SMEs).

Approximately 20% of the social enterprises that existed five years ago, roughly 700, have since ceased operations, mostly because their business models were unsustainable. This compares favorably to the 38% average default rate for SMEs over five years. Potential explanations are social enterprises' access to donations and concessionary funds that help them survive difficult periods as well as the extraordinary drive to create impact that keeps social entrepreneurs engaged even when business is not going well.

¹ We estimated the number of social enterprises for 2016 and 2011, but based the employment and revenue data on our survey data where we asked the respondents to reflect on their figures in 2010 and 2015. The CBS data for reference is also available for 2015.

As a result of the overall growth in the number of enterprises since 2011, the average stage of growth of social enterprises is low. About half of our survey respondents said they were in the early-stage growth phase and 20% in seed or start-up phases.² This means that only about 30% are in later stages of growth.

Stages of growth before maturity

- 1. Seed phase:** (0-2 years) The founding team develops the idea and translates it into a prototype product or service. Prototype funding comes from founders' resources and/or contributions from friends, families and crowdfunding.
- 2. Start-up phase:** (1-3 years) The team develops the prototype and brings it to market. A customer base is established and KPIs are identified. The enterprise receives its first revenues and attracts additional resources in the form of investments or loans.
- 3. Early-stage growth:** (2-5 years) The enterprise aims to increase its scale through new channels and markets. It hires talent, improves quality and implements standard management processes. Funding comes from revenues and growth capital.
- 4. Later-stage growth:** (>3 years) Having established a reputation with stakeholders, the enterprise looks for additional growth beyond the initial products or services. Several capital options are available. Some founders and/or investors may make exits.

Societal awareness and development of infrastructure brought new attention for social enterprises

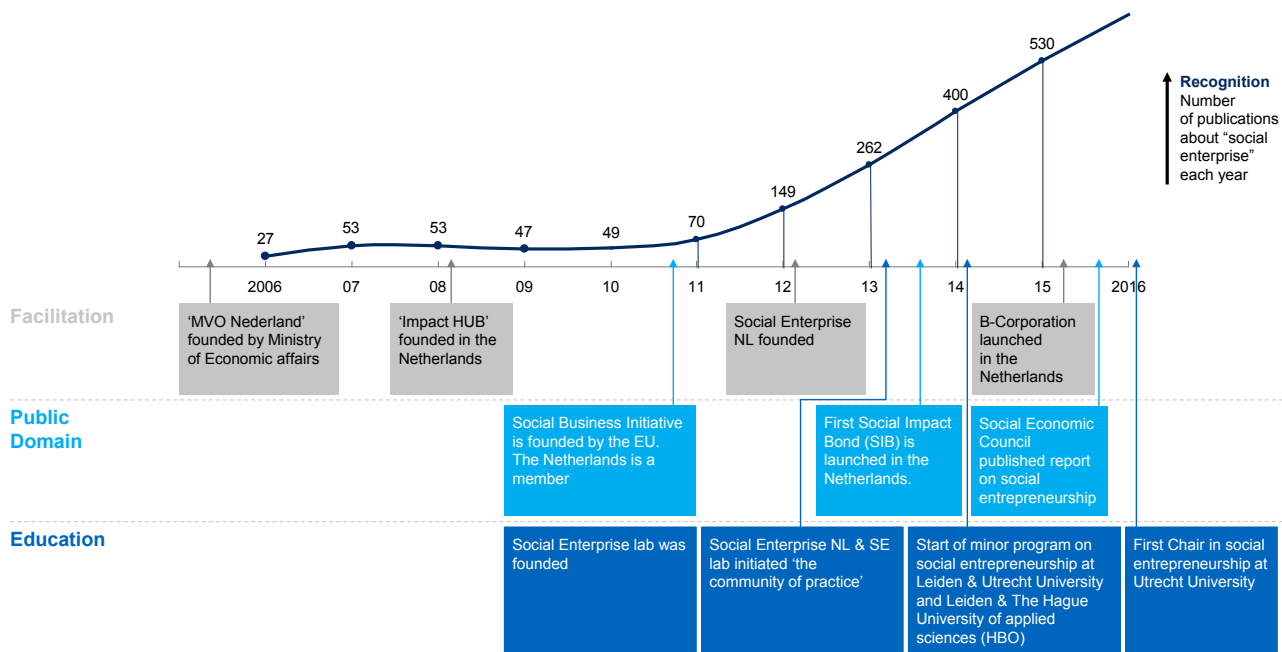
Many trends and developments indicate an increased emphasis on social impact as a goal and social entrepreneurship as a means to that end. The sector became more visible, thanks to increased publications and media attention. The sector's profile also rose because of general societal trends and specific advances in infrastructure and education.

Consumers today are more conscious of health and the environment, for example. More people, especially millennials, are willing to accept lower incomes to pursue social impact, and most traditional corporates now include CSR in their core business initiatives and report more transparently about it, in part to comply with new legal requirements (Exhibit 3).

Over the past five years, infrastructure has expanded to serve about 4,000 social enterprises. Five new network platforms were established to support social enterprises, and up to 40 competitions, accelerators and incubators have started. To date, however, 37% of social enterprises responding to our survey said that they are not making use of this infrastructure.

² We manually adjusted the distribution of our sample to account for the underrepresentation enterprises in seed and start-up phases, as well as some of the largest mature enterprises. This provided more accurate total revenue and employment estimates.

Exhibit 3: The development of Dutch social enterprise infrastructure

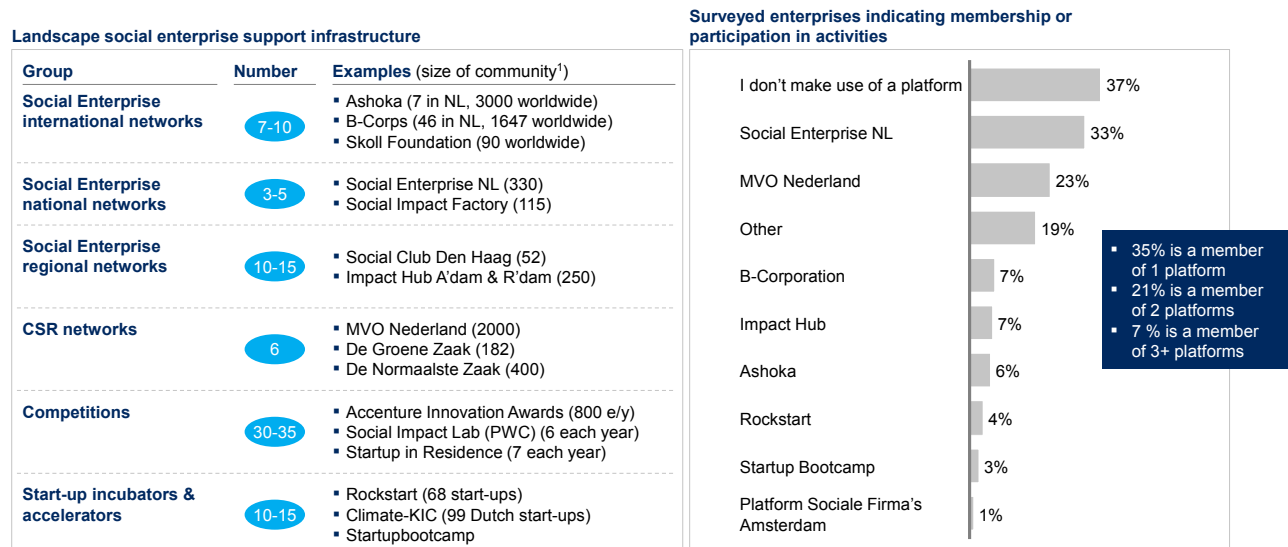


Some do not see value or relevance of support platforms and incubators, and others are unaware of their existence or use alternatives, such as traditional local business networks.

At the other end of the spectrum, more than 25% of the respondents said they obtain support from two or more facilitators. All platforms offer at least light support and network events; some also provide funding or workplaces. A few, like Social Enterprise NL, also lobby the government for recognition. Most platforms focus on early-stage growth companies, although the competitions, incubators and accelerators target seed and start-up enterprises as well. The target audience of most CSR networks is mature companies, although the other platforms are also increasingly addressing the needs of entrepreneurs beyond the early stages (Exhibit 4).

In the public domain, social enterprises are receiving increasing attention from the national government and municipalities. Especially at the local level, civic and government leaders recognize social enterprises' potential to help address issues in a sustainable way. Amsterdam and Utrecht, for example, have introduced action plans ranging from facilitating work spaces to investigating opportunities for procurement. Even in early stages, these plans and programs promise stimulating measures and support. At the national level, a report from the Social Economic Council included clear recommendations for the government to improve the financing climate, invest in impact measurement and increase awareness about social enterprises among civil servants.

Exhibit 4: Landscape of social enterprise infrastructure and membership



¹ Not exclusively social enterprises

SOURCE: McKinsey Social Enterprise survey (N=182)

Higher education institutions have also begun to address social entrepreneurship. Six universities and six higher education institutions have created minor programs and courses focused on social entrepreneurship. Hogeschool Rotterdam, for example, now offers a bachelor's degree in Marketing of Social Business. While these schools teach specific social entrepreneurship skills, more schools of all kinds are helping students learn basic entrepreneurship skills.

Social enterprises focus on impact areas while being active in diverse industries

In this report, we distinguish between industry and impact area. By 'industry', we mean areas of economic activity, which could include multiple products or services. By 'impact area' we mean the primary way an enterprise strives to create social value and/or solve a societal problem. These impact areas are what distinguishes social enterprises from other businesses.

Industries

The social enterprise sector consists of a highly diverse group of organizations in a broad range of industries. The largest group of social enterprises serves the 'health and well-being' industry (31%), followed by 'energy' (17%) and 'financial and business services' (16%). More than 41% of the enterprises are active in two or more industries (Exhibit 5).

Impact areas

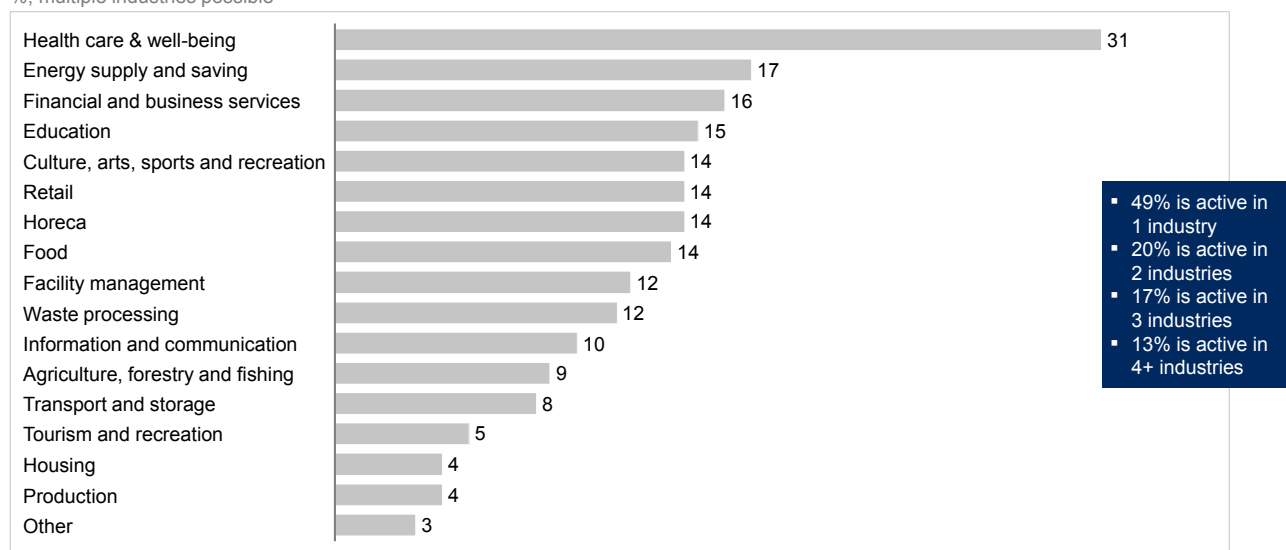
Social enterprises have a mission to solve societal problems or create social value. Their activities can be grouped into seven impact areas where all 17 UN global development goals are addressed, along with important Dutch societal issues. This report defines the size

per impact area based on enterprises' primary goals. The two impact areas where social enterprises are most active are 'stimulating the circular economy' (25%) and 'increasing labor participation and equality' (20%). The two smallest impact areas are 'international development' (8%) and 'education' (7%), although these attract more interest as secondary goals (Exhibit 6).

Exhibit 5: Industries in which Social Enterprises are active

In which industries is your enterprise active?

%, multiple industries possible



SOURCE: McKinsey Social Enterprise survey (N=182)

Exhibit 6: Size of impact areas

Impact area	Examples	Company examples	Company goal ¹		Started last 5 years	
			Primary %	Secondary %	Primary %	Secondary %
Stimulating the circular economy and renewables	<ul style="list-style-type: none"> Stimulating affordable sustainable energy (sources) Enlarge sustainable energy production and consumption Recycling of natural resources Sharing of goods and services Combating climate change 	<ul style="list-style-type: none"> Afval loont Rotterzwam VandeBron 	25	11	29	
Enlarging labor market participation & equality	<ul style="list-style-type: none"> Enlarging labor market participation Stimulating gender equality on the work floor 	<ul style="list-style-type: none"> De Prael De Meewerkers 	20	15	23	
Improving health and well-being	<ul style="list-style-type: none"> Improving health care Stimulating health lifestyle and (emotional) well-being 	<ul style="list-style-type: none"> WebChair Woonz 	14	10	22	
Promote social cohesion	<ul style="list-style-type: none"> Enlarging of social cohesion in the neighborhoods Aid social integration of refugees Renew existing infrastructure for mobility 	<ul style="list-style-type: none"> Peerby Refugee company 	12	10	10	
Improving the food chain	<ul style="list-style-type: none"> Stimulate local or organic production of products Stimulate traceability of the food chain Advance clean drinking water and sanitary facilities 	<ul style="list-style-type: none"> Koppert Willem & Drees 	10	7	8	
Stimulating international development	<ul style="list-style-type: none"> Stimulating economic growth or fair working environment Fighting hunger Preventing armed conflicts Innovate industries and infrastructure Founding and improving of institution 	<ul style="list-style-type: none"> Waka Waka Fairphone Text to Change 	8	13	4	
Improving education	<ul style="list-style-type: none"> Stimulation of new and qualitative good education 	<ul style="list-style-type: none"> Codename Future ToWatch 	7	9	4	
Other		<ul style="list-style-type: none"> 1% Club 	4	2	1	

¹ Based on number of Social Enterprises

SOURCE: McKinsey Social Enterprise survey (N=182)

Each primary impact area is growing at a different rate, based on the number of companies started within the last five years. The three largest impact areas attracted more start-ups, for example.

Growth in circular economy and renewable energy is largely driven by IT-enabled platforms building on AirBnB-like websites and sharp declines in the cost of solar and wind energy. Labor market participation enterprises grew thanks to the participation legislation, which increased the need for solutions (i.e., sociale werkplaatsen being privatized). The growth in health and well-being accelerated as legislation permitted more flexibility, resulting in more open market conditions.

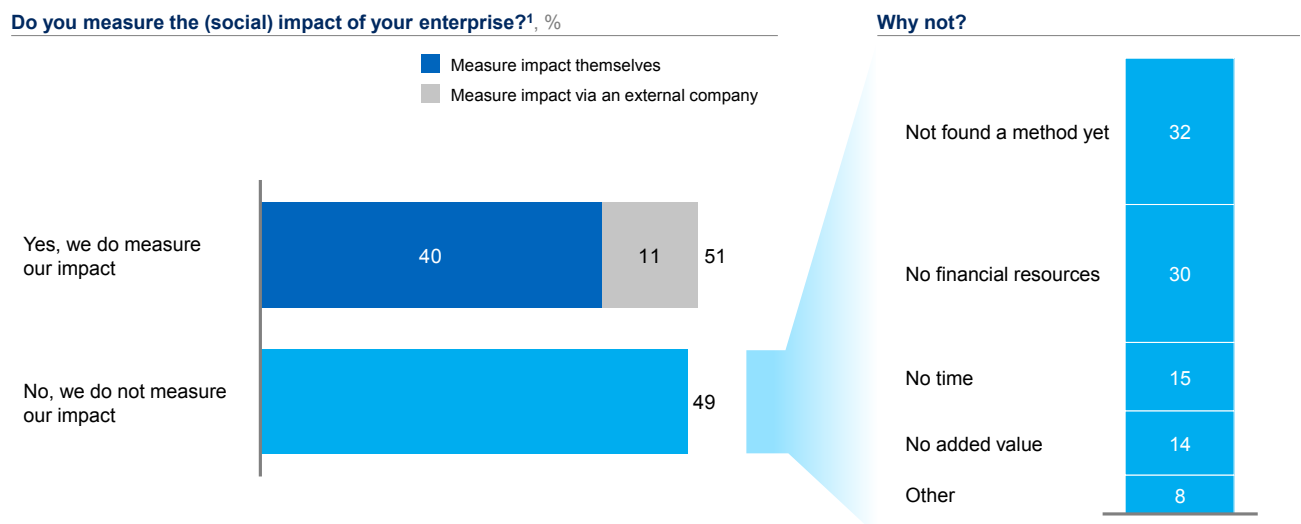
3. Impact and financial performance of social enterprises

Measuring impact remains difficult

While the sector’s employment and revenues are growing, even rough impact estimates are not yet available. Barely half of social enterprises measure some form of impact, and 35% measure a relevant unit, such as CO2 emissions. The other half do not yet measure their social impact. Impact can be measured in different ways, from relatively simple calculations of input, activity and output to more relevant but more complex measures of outcomes.

Most of the enterprises that do not measure impact have yet to find a good method or do not have the financial resources to measure their impact. Of the enterprises that do measure their impact, 11% do so through involvement of external companies (Exhibit 7).

Exhibit 7: Impact measurements



¹ 6% percent of the people did not know if they measure the (social) impact
 SOURCE: McKinsey Social Enterprise survey (N=182)

In a segment where adding social value is the single differentiating factor, impact measurement is the currency of the sector’s value. Lacking standards for impact measurement, the absence of an impact measurement infrastructure, and high measurement costs for individual enterprises create obstacles for social enterprises individually and for the sector as a whole.

On an enterprise level, impact data would enable business feedback and improvement, and it could help to secure contracts and capital. On a sector level, impact measurement could increase the visibility of social enterprises and help them attract more entrepreneurial management and technical talent.

Output as an alternative for impact

The low involvement of enterprises in impact measurement and the diversity in measurement methods make it impossible to estimate the sector's total impact. Every impact area has its own key indicators, many of which cannot yet be translated in a single unit, such as monetary value.

Output can be quantified in some impact areas, giving a rough initial proxy of total impact realized by social enterprises. Three examples:

- **Labor market participation:** About 1 million people in the Netherlands are labor disadvantaged through a physical, mental or sensory limitation, of which approximately 40% work. About 30,000 disadvantaged people are employed by social enterprises representing almost 10% of available jobs. In addition to reducing government spending on care and welfare, the impact for society comes mainly from raising these people's self-esteem and providing them with social networks and opportunities to contribute. Enterprise examples include Brewery de Prael, Emma Safety shoes and Kringloopwinkels, with varying labor intensity from the disadvantaged employees, ranging from assisting to full-time jobs.
- **Renewable energy:** The Netherlands aims to generate at least 14% of its energy from renewable sources by 2020, up from only 6% today. Social enterprises produce about 10% of the renewable energy in use today, contributing substantially to the government's commitment. Some of these players can compete on price with the big energy corporates because they accept lower profit margins thanks to their 'impact first' mission. Examples of enterprise players in this market are Vandebron and Current at the national level and Texel Energy at the local level.

Van de Bron: The mission of VandeBron is to move as fast as possible toward 100% sustainable energy by connecting consumers directly to producers of clean energy. The group's online marketplace brings many small players together to create the scale to be relevant in the market. So far, the company provides over 80,000 households with access to clean energy.



© www.vandebron.nl

- **Refugee integration:** Integrating refugees is a major issue within social cohesion today. The UNHCR reported that the Netherlands was home to about 82,000 refugees in December 2014, and that about 59,000 entered in 2015. So far, social enterprises such as New Bees, Refugee Company and TakecareBnB have helped around 3,000 refugees integrate in Dutch society.

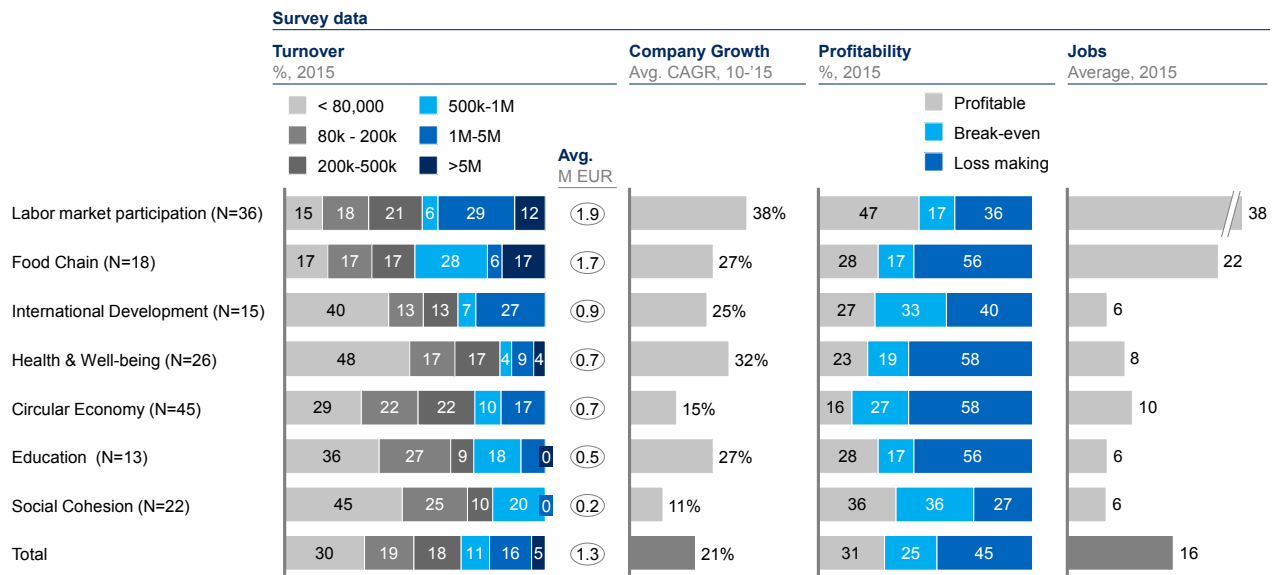
Fewer than one in three social enterprises is profitable

The financial performance of social enterprises falls behind that of for-profit companies, as 31% of survey respondents reported profits in 2015 versus 51% for the overall Dutch economy. About one in four social enterprises is breaking even and 45% are making losses. Part of the shortfall can be explained by the fact that about 75% of social enterprises are in the seed or start-up phases. Of those younger than three years, 60-70% are recording losses.

Surveyed enterprises generated an average of 1.3 million euros in revenue in 2015.³ About 30% reported revenues of less than 80,000 euros, and about 20% more than 1 million. The average enterprise grew revenues by about 20% annually over the past 5 years.

The average financial performance of social enterprises varies significantly by impact area. The areas with the largest revenues are 'labor market participation and equality' and 'improving the food chain' with 1.9 million and 1.7 million euros in revenues and 38 and 22 employees respectively. 'Labor market participation and equality' shows the largest annual revenue growth of 38% as well as highest percentage of companies reporting profits. The impact areas with the lowest revenues are more locally focused, such as 'social cohesion' and 'education' initiatives (Exhibit 8).

Exhibit 8: Results by impact area



SOURCE: McKinsey Social Enterprise survey (N=175)

³ This estimate for the sector is based on the survey responses, but the tail from start-ups and the largest companies are underrepresented in the data sample.

The potential for growth is determined by two broad archetypes

Analyzing variations in performance and ambition, we found two broad archetypes:

1. Community enterprises: Many enterprises aim to create local impact without ambitions beyond their immediate communities. We found this archetype mostly where the government has pulled out or cut subsidies, for instance where the semi-public care system cannot meet all needs or in rural areas where jobs are scarce. Many of these enterprises are legally registered as Stichting. Although their individual growth ambitions and scalability are limited, their collective impact is substantial. According to the social enterprise monitor 2015⁴, about 70% of the founders of community enterprises have at least five years of working experience.

Examples of community enterprises are Bloesem Theehuis, Buurtkamer Corantijn and MidWest, who conduct activities formerly coordinated or executed by municipalities. Their activities serve an important community function and they are partly run by volunteers. This exemplifies what is considered a value of Dutch society, namely that everyone takes responsibility for their community ('participatiesamenleving'). Many small social enterprises together create substantial impact.

2. Society changers: Other enterprises compete more directly with commercial companies. They aim to change the market by incorporating impact in the value chain, often by innovating, such as platforms that use IT to create scale by linking customers to small businesses. Their impact depends not only on the company size and activities (direct impacts), but also on their effects on society and the market (indirect impacts). Social enterprises aim to deliver both, but depending on their ultimate ambition and scale, they can be classified as either 'step-changers' whose main impact is direct or 'systemic changers' whose impact is mainly indirect. Our research showed that younger entrepreneurs are more likely to found society-changers.

Step-changers include Videobutler, Bright Pensioen and De Buurtboer. Enterprises as Fairphone and Tony Chocolonely were initially step-changers but after growth and strategic repositioning increased their attributed impact, making them systemic changers now. However, not all systemic changers achieve indirect impact as a result of their own scale; Taxi Electric, for example, lost the Schiphol tender after lobbying for social criteria in the procurement process but still changed the taxi market. Similarly Specialistterren is still relatively small, but by proving that autistic workers could master software testing, they made a major contribution to solving part of the labor participation issue.

Differentiating among these archetypes can help reveal challenges and growth opportunities.

Impact investment spectrum narrows relevant capital scope

Unlike traditional companies, many social enterprises have access to capital dedicated to creating a positive impact on society and environment. Philanthropic and public sources used to provide these funds, but new sources are becoming available as 'impact investing'

⁴ Social Enterprise NL, underlying survey data to 'Social enterprise Monitor 2015'



gains traction. Impact investors aim to combine measurable social and environmental advances with financial returns. They differ from traditional investors in terms of their risk/return objectives, impact characteristics, sector focus and deal sizes (GIIN, 2016).

We see two broad types of impact investors:

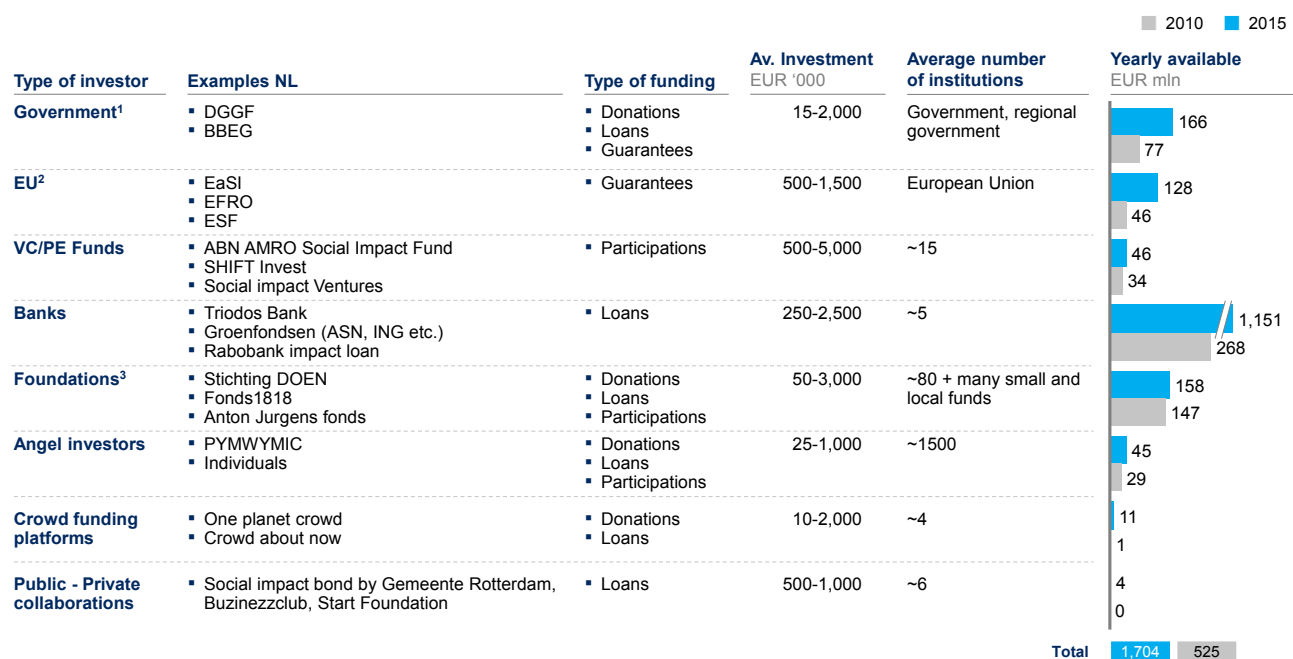
- Those aiming for risk-adjusted market-rate returns, such as banks and venture funds
- Those willing to accept concessionary, below-market financial returns, higher risks or longer investment horizons in exchange for impact, such as philanthropic foundations and angel investors.

Three times more capital is now accessible to social enterprises

Social enterprises prefer to obtain capital from mission-aligned investors, but many also tap traditional financial sources. This report focuses on capital specifically accessible to social enterprises and has sized the capital sources that aim to maximize impact with or without a profit.

Financial providers tend to look more closely at a company's intentions than whether it is a social enterprise. The capital available mapped in is thus available to both social enterprises and other impact-driven enterprises (Exhibit 9).

Exhibit 9: Capital accessible to social enterprises per investor type¹



¹ Estimated share of funds accessible to social enterprises (and other impact focused companies)

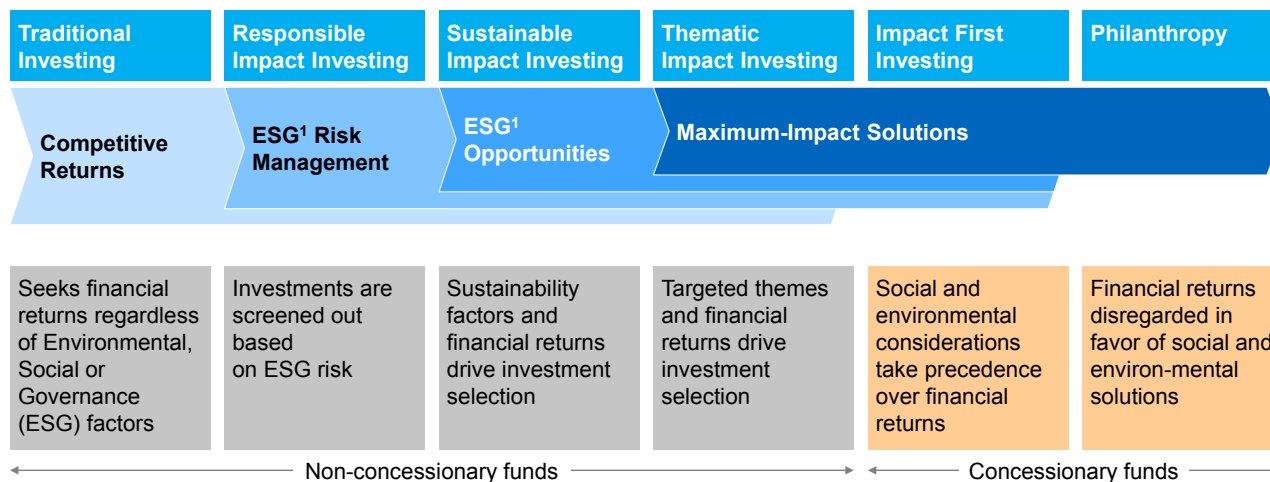
² Available via Dutch government agencies and financial providers; ³ Includes Family Offices

SOURCE: Annual reports of banks and foundations, websites of banks, funds, foundations, Douw&Koren, Panteia, BAN, EU, SIBs, expert interviews, NL government budget

The amount of capital available to social enterprises (and other impact investments) has tripled since 2010 and is therefore now no longer short, although not all capital finds its way to these enterprises. Some professional, impact-oriented financial providers have difficulties allocating all the capital in this segment, for example, and therefore invest some of it in companies with an environmental, social and corporate governance (ESG) profile more to the left of exhibit 10. All identified sources have increased the amount of capital dedicated to impact, and new players have added to the pool of funds available. Crowdfunding, for example, has proven to be a valuable yet still small source of funds for social enterprises. One Planet Crowd is an example of a dedicated impact crowdfunding platform.

An increasing number of angel investors are active in the Netherlands (Panteia, 2014), including a group targeting social enterprises. Moreover, according to research in 2014 by ABN AMRO, a large share of informal investors have shown interest in impact investing. Philanthropic foundations show a similar trend, and traditional financial institutions such as Rabobank and ABN AMRO are starting to experiment with impact investing. More impact dedicated capital has become available from banks thanks to the growth of Triodos Bank and the launch of 'Groenfondsen' such as ASN Groenprojectenfonds and ING Groenbank. However, as only a limited amount of social enterprises is eligible for bank financing, most of this impact dedicated capital goes to ESG practices of more traditional companies.

Exhibit 10: Overview of the financing spectrum by level of impact and financial returns



¹ ESG: Environmental, Social and Corporate Governance
 SOURCE: Sonen Capital & Bridges Capital & Clara Barby

The professional investment landscape has seen successful launches of dedicated impact funds such as SI2 and Social Impact Ventures. Few impact funds today focus on a specific impact area, although some specialized funds such as SHIFT Invest and Triodos Organic Growth fund pursue cleantech and agricultural themes. Specialization may increase as the social enterprise market develops.

The Dutch government, rather than targeting social enterprises directly, is adopting impact themes such as sustainability in its policies and subsidy programs. The European Union provides funding to stimulate social entrepreneurship in member countries, which is accessible for social enterprises via local investment funds and the national government. Nonetheless, the Netherlands is not making optimal use of these EU-specific resources yet.

Social entrepreneurs encounter a wide range of investors along their growth path

Over the lifetime of a social enterprise, different financial actors play a role. Exhibit 11 shows the most-used capital sources by social enterprises per investment stage (see page 6 for definitions of stages of growth) and highlights which investors aim more for market-based financial returns or take a concessionary approach.

Most funding in the seed stage is provided by friends and family, while foundations and angel investors invest more during the startup stage. In the growth stage, enterprises tap more professional sources, such as venture funds and banks. Crowdfunding can work in all phases, while the government indirectly supplies financing via subsidies and guarantees.

Exhibit 12 on the next page displays the frequency of types and sources of capital as indicated by our survey respondents; the figures do not indicate relative weight.

Exhibit 11: Overview of investment types available per phase and investment amount

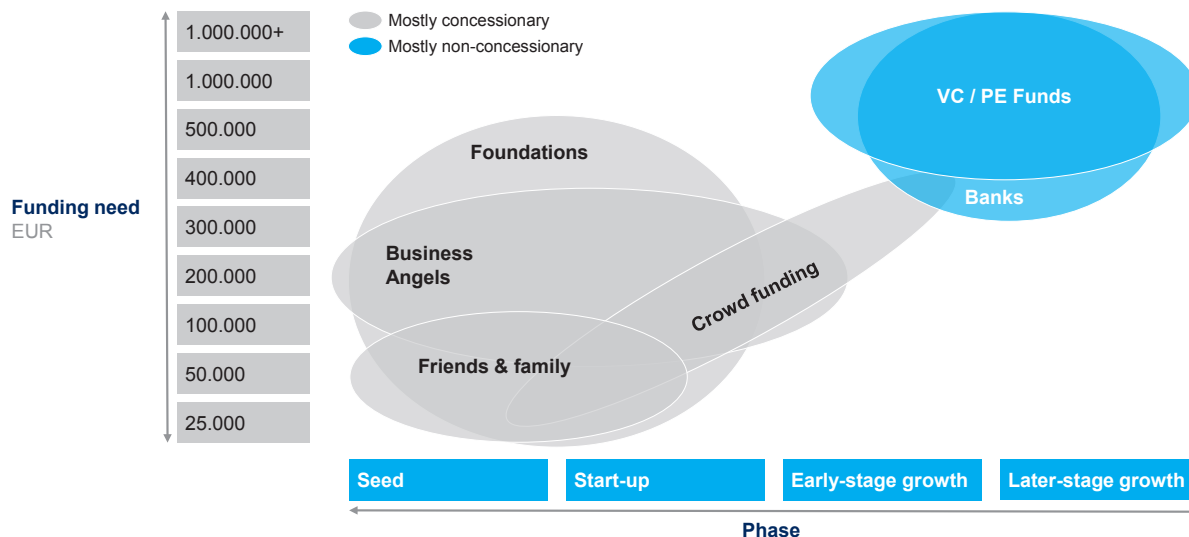
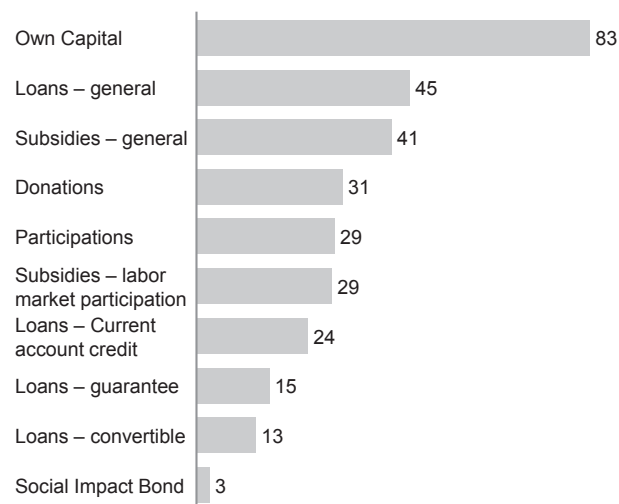
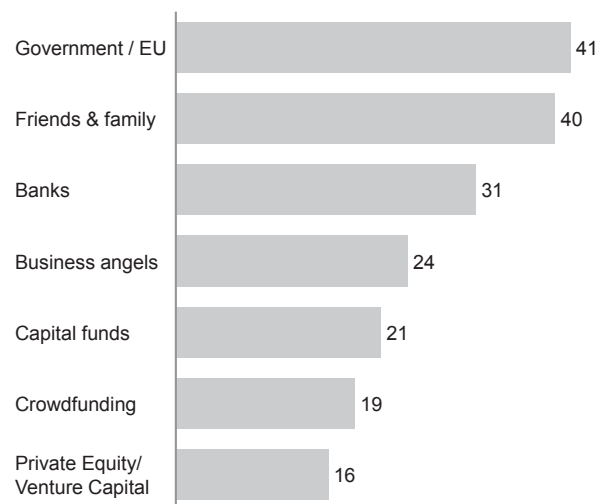


Exhibit 12: Types and sources of capital for social enterprises

Types of financing used by social enterprises, %



Categories of sources providing financing for social enterprises, %



SOURCE: McKinsey Social Enterprise survey (N=182)

The largest types of financing next to owners' equity (83%) are loans and general subsidies. Most subsidies used by social enterprises are not impact-specific; the WBSO innovation subsidy, for example, is used by many innovative social enterprise startups. The least common financing type is relatively new: social impact bonds.

The most commonly providers of external financing, both mentioned by about 40% of respondents, are friends and family and the government, although its subsidies and guarantees are not fully comparable to more standard forms of financing.

Capital is not evenly distributed to impact areas and archetypes

Despite the work of some generalist impact funds, most capital is still directed to environmental themes such as renewable energy, agriculture and now circularity. Many banks have a 'Groenbank' facility available for social enterprises, and most government impact-focused subsidies target renewable energy and sustainable agriculture. For labor participation, specific government subsidies are available.

Community enterprises find it particularly difficult to get access to capital because the payback period on their investments can be long. These typically unscalable initiatives may be run by volunteers or local cooperatives with little or no capital of their own and low growth ambitions. According to a report on impact financing⁵, commissioned by Ministry of Internal Affairs, community enterprises need credit of at least 200 million euros to achieve their goals.

Capital and coaching are in short supply in early phases

Many social enterprises find it difficult to secure enough capital in their startup and early growth stages. They tend to be less profitable, and many are still perfecting their business models to drive growth. In other words, they need in-depth coaching and counsel in addition to capital.

The likely sources of capital in earlier stages, such as crowdfunding, foundations and government subsidies, may not have the capacity or knowledge to provide extensive business support. Many hands-on equity investors do offer guidance, but mainly to more mature enterprises. This is a fundamental problem, because below a threshold of about 400,000-500,000 euros, the costs of due diligence and support exceed expected returns by a wide margin. Angel investors may offer access to their network and some level of support but generally have limited time and cannot meet all demand.

This gap in 'professional funding' forms an obstacle for social enterprises in the start-up and early growth phases. In particular, these enterprises have difficulties obtaining working capital and must sometimes tap equity instead.

⁵ TwynstraGudde 2016, Report title 'Samen maatschappelijke impact financieren'

4. Vision for the social enterprise sector

Social enterprises gained popularity at the beginning of the financial crisis in 2008, and their appeal has grown in the past five years along with media attention, the number of enterprises, jobs and revenues. Capital has flowed into the sector, support platforms emerged, research and education began to address the topic, and municipalities began developing programs. Despite this growth, however, most social enterprises and the sector as a whole are still in the early stages of development.

McKinsey’s vision for the social enterprise sector is to grow the impact of the sector fivefold in the next five to ten years (Exhibit 13). To achieve this scale-up of growth, the sector needs to professionalize on multiple dimensions.

Exhibit 13: The social enterprise sector can scale impact through professionalization



Professionalization can accelerate growth in existing social enterprises and inspire new entrants in different ways. First, community enterprises can replicate their success by franchising and sharing best practices. Second, society-changers can attract more talent to improve their success rates. Third, platform organizations can help create scale for and access to social producers and service providers. And last, the largest opportunity for growth might be found as existing SMEs and corporates shift to the left side of the impact spectrum, increasing their CSR activities or even becoming social enterprises – a shift we expect from family enterprises in particular.

Enterprises will need more talented, experienced entrepreneurs. Capital providers will need to offer more innovative financial solutions and make early investments based on more critical assessments, and pair those investments with professional coaching and support. Support networks have boosted the early phases of growth, but a professional (and financially independent) market needs to develop to provide the next level of

professional facilitation, including specialized financial support and longer-term critical business plan coaching. National and local governments should increase recognition for the sector and offer more opportunities to boost development. As its impacts become more visible, the sector will inspire more support from society to boost its scale and accelerate professionalization – a precondition for the next level of growth.

Kromkommer

About 10% of fruit and vegetables are wasted because of looks or overproduction. Kromkommer aims to change this quality perception from worthless to loveable. They do this with positive, creative campaigns and their own line of soups for sale in 150 stores. So far, they have inspired supermarket Jumbo to make similar soups and Albert Heijn to sell fresh 'wonky' produce.

De Groene Grachten

Co-founder Wubbo Ockels, a late Dutch astronaut, explains the organization's mission: 'We are all astronauts of the spaceship earth. The only future is a sustainable future.' De Groene Grachten (the Green Canals) does this by making old buildings sustainable. It shows how a team of young entrepreneurs can include join forces with a more experienced visionary leader to start a successful company. They are working on dozens of projects throughout the Netherlands to create sustainable historic buildings.

5. Challenges for professionalization and further growth

We identified five main challenges for professionalization and further growth of the sector in the next five to ten years. In this section we list these challenges, in the next section we present our recommendations.

1. The sector and its stakeholders focus too little on scaling up

Many stakeholders believe that the missions of social enterprises may not include revenue or profit generation. Specifically, profit generation and social values are often perceived as incompatible priorities. But to increase social impact, enterprises need to scale up. That requires revenue growth ambitions from entrepreneurs, public acceptance of profitability and even dividends large enough to attract talented entrepreneurs, government recognition and professional financing and support.

2. It's difficult to attract management talent for the next stage of growth

Like traditional start-ups, social enterprises struggle to attract sufficient management talent as they grow. Founders can often rely on charisma and enthusiasm to get an organization off the ground, but reaching the next stage of growth requires specific operational and financial expertise. Attracting people with those skills takes time, and many enterprises find it difficult to attract experienced people for management positions, since they tend to pay less than in commercial enterprises.

3. 'Friendly but lazy' money decreases the urgency of growth

Social enterprises in the seed and start-up stages have access to concessionary capital such as crowdfunding and foundation grants. This access to friendly money in the early stages without sufficient pressure to achieve scale prevents many enterprises from adjusting their business plans accordingly.

Many of those who do want to scale can gain access to the next level of funding of 50,000-500,000 euros, but few funders in this range have the capacity, expertise, investment models or knowledge to provide the intensive business support or coaching that social entrepreneurs need to scale up their business. This gap in 'professional funding' forms an obstacle for social enterprises to grow beyond the start-up or early growth phases.

Venture capital and private equity firms, banks and hands-on equity investors willing to provide more than 500,000 euros do offer intensive support, but few social enterprises become large enough to be attractive to these kinds of capital providers. Below investments of 500,000 euros, the costs of professional support cannot be compensated by the expected return.

4. Limited standardized impact measurements hinder tracking and comparisons

Many social enterprises do not measure impact. Others use a wide array of different impact measurement methods, and few investors request systematic, standardized impact measurements. It is therefore difficult to quantify or compare the impact of individual enterprises or the sector as a whole, which in turn limits its visibility and its ability to attract talent, funding and government support.

5. Buying from social enterprises not yet widely seen as a priority

Creating enough demand is one of the main prerequisites for driving growth. Although public-sector organizations and commercial enterprises pursuing CSR would benefit from social procurement, only a few have decided to include social impact criteria in their procurement processes.

6. Opportunities and recommendations for sector growth

We believe that to realize impact at scale, the next step for the social enterprise sector is professionalization. In this section we present our recommendations and suggestions for addressing the challenges presented in the previous chapter, and we outline some of the opportunities for growth that emerged in our research. Most of these suggestions involve multiple stakeholders:

1. Focus more on scaling impact to make the sector more attractive to investors, talent, civic leaders and other stakeholders

The focus in and around the sector should be more on scalability as the key to expanding social impact⁶. By stimulating more positive attitudes towards revenue growth, profitability and even dividends, the sector will attract more talent and other stakeholders who will stimulate scalability. Government, support networks and investors could contribute by sharing more of what they know about successful social enterprises. This will increase awareness that scalability and social impact go hand-in-hand.

2. Attract, develop and retain management talent to build enterprise teams for growth

Entrepreneurs should promptly invest in new talent with the management competencies necessary for professionalization and scale-up as well as in developing, training and retaining employees; and professional coaching and support. Investors and support networks can help entrepreneurs and their development by offering support, network opportunities and training across each stage of growth.

Furthermore, corporates can help enterprises improve their management skills by institutionalizing coaching, knowledge- and skill-sharing through secondment programs, where corporate talent can take sabbaticals to join a social enterprise.

3. Professionalize investor and capital provider support

Venture capitalists, private equity investors and banks could offer more innovative financial solutions and could co-invest with philanthropic foundations, angels or crowdfunding platforms to provide life-span financing and capital continuity.

To increase professionalization of funding, capital providers could specialize on fewer or subsets of industries and/or impact areas. This will help them assess risks, provide more tailored support and boost collaboration among capital providers.

4. Create standard impact measurements to improve visibility of sector

The sector must create practical, off-the-shelf methods for measuring impact in each area and phase to increase visibility and impact. Promulgating these methods will require training and how-to guides. Universities can play a leading role in setting up these methods through partnerships with capital providers.

Investors and incubator and accelerator programs should give enterprises incentives to measure impact by including the metrics in financing criteria and providing financial support based on impact.

⁶ This recommendation is focused on society changers enterprises. For community enterprises scaling impact should happen through focusing on duplicating initiatives rather than revenue growth.

5. Include impact criteria in procurement processes to increase demand

Government as a large buyer of goods and services should take the lead in defining and implementing joint social impact criteria. The semi-public sector and ideally corporates should include these criteria in their procurement processes. For the public sector, the G32 network could help accelerate the roll-out of these criteria across Dutch municipalities.

Furthermore, enterprises should lead, in collaboration with corporates and the public sector, the set-up of social sourcing collaborations to make enterprises' products and services more widely accessible.



Ultimately, the value of the sector lies in its social impact. And while the Dutch often judge success critically, they will need to celebrate successful social entrepreneurs. The social enterprise sector can play a pivotal role in balancing profit generation and social values.

Acknowledgments

We are grateful to all who helped us write this report through insightful conversations, passionate challenges, and access to information and personal networks:

Aart van Veller, Anja Steentjes, Bart Lacroix, Bjorn Vennema, Ellen Oetelmans, Fer Kok, Ineke van Zanten, Jelle Rademaker, Jiska Klein, Jørgen van Rijn, Joyce Knappe, Laura Cramer, Maarten van Dam, Machtelt Groothuis, Marieke Kamphuis, Mark Hillen, Martin Koppert, Niels Bosma, Paul Thewissen, Peter Hobbelen, Pieter Oostlander, Raphael Nouwen, Rinske van Noortwijk, Saskia Werther, Tatiana Glad, Toke Tom, Wendelien Hebly and Willemijn Verloop