

A Brief Institutional Analysis on Social Businesses as Option for Start-Ups in Nepal

ABSTRACT

Social business is a new phenomenon in Nepal as well as in most other countries of the world. Yet if we have a look at the social business landscape it is more small isolated islands of one or a few socially responsible businesses, social businesses and NGOs with revenue models we find rather than a real scene.

Among the organizations which developed so far, we can find a majority of working on employment generation, even though only few of them are active in the underdeveloped rural areas, where the social return per job created would be relatively higher than in the already dense urban setting.

The way, how each of them brings change to the communities differs from organization to organization. Product oriented social business approach their social target group as their customers, employment oriented want to bring change through their employees and environmental oriented work towards the less tangible vision of a less polluted Nepal.

As no standardized measurement tool has been applied so far, it cannot be analyzed currently if those organizations outputs – which equals their ability to consequentially solve the social problem they tackle – eventually creates the intended change in the society.

In any case social business needs to be designed as such from the beginning onwards so that more potential lies in start-ups and new initiatives choosing this option. Even though some first supportive structures emerge in different sectors such as a legal entity or scattered efforts of incubation, does the current institutional situation not favour new social business on a bigger scale. Not only are hardly any specific supportive structures in place but also general settings, such as the lack of rule of law which makes many business fields very unhealthy, are rather hampering social business start-up.

1 Introduction

Food adulteration, corruption, brain-drain, pollution and malnutrition; the list of social issues in Nepal is long. Despite fertile land, plenty of water sources, gorgeous landscapes and a rich history, which attracts tourists from all over the world, neither the private sector of Nepal, nor the government (with plenty international support) has been able to unravel the situation so far. In opposite; there is rather evidence that several problems are caused by the inability of the government to provide social services and by an unethical behaviour of the private sector (NBI, 2013).

Many scholars call for a more human centred (Felber, 2012), localized (Norberg-Hodge, 2001) (Hopkins, 2013) and prudent (Sukhdev, 2012) behaviour of businesses and critically review economization of the society (Costa, 2010). Social business as an idea provides a new approach to these issues by being able to make social services self-sustainable and business creating more positive impact on society.

Social businesses can emerge from different starting points, such as NGOs turning towards more financial sustainability or a traditional cooperation, running a less profitable social business as one of the daughter companies. Yet the majority of new (social) businesses are start-ups, which means that the founding team starts off from zero.

This paper tries to briefly review the social business scene and shine some light on the context in which it operates. After a short initial discussion on a typology of social businesses the paper will review the institutional setting in which the social business start up scene operates and indicate some reasons, which hamper the emerge of social business on a bigger scale.

2 Refining the picture: A Social Business Typology

Professor Yunus defines a social business as an organization following seven principles¹. The way they are formulated they are a powerful value framework, yet they provide less operative guidance or granularity for a scientific analysis. This chapter review existing models and introduce a new typology to categorize social businesses from a very pragmatic perspective.

Kim Alter (2015) has done considerable ground work and identified nine fundamental models of social enterprises as well as a variety of complex models, combining two or more fundamental models with each other. This approach is very valuable to understand all form of hybrid organizations, including socially responsible businesses and NGOs with profit making models, which do not necessary align with the seven principles. Yet there are two reasons this model could be improved from the perspective of a start up: Firstly it has several complex models,

¹ The seven principles of Prof. Mohammed Yunus can be summarized as an organization which is having same like a NGO the social objective first, yet is same like a business sustainable in its work, while being environmentally friendly and providing better working conditions to the workforce than traditional businesses. For the full list of principles see <http://www.grameencreativelab.com/a-concept-to-eradicate-poverty/7-principles.html>

which are normally not relevant for start-up and make it unnecessary complex therefore and secondly it does not allow for an environmental driven social business.

Another approach was developed by Christian Felber and a group of reflective business persons from Europe. It is called *common good matrix* and strives to capture the social impact a business has on its different stakeholders. Therefore the model assesses the values in relation to these stakeholders, such as solidarity, democracy and ecological sustainability. (Felber, 2012) Yet this model is not made for social businesses in particular, but for assessing the social impact of any arbitrary business and starts from an assumption of a neutral social impact, so that the matrix is not immediately useful for guiding and categorizing start-ups.

Yet combining the idea of different types of social businesses and fusing it with the stakeholder and value idea of the common good matrix, we can derive a simplified typology which proved useful for the incubation of social business start ups in Nepal as shown in Figure 1.



Figure 1 Typology of Social Business

Social businesses of the Type A approach their beneficiaries as their customers. This customer can either be from the so called bottom of the pyramid (BoP) or a product or service for a group with a special need (i.e. books for blinds). Products or services for such social businesses will have a different design and especially for BoP products lower margins and require special arrangements for the distribution channel.

Social businesses of Type B are striving to create their impact through their employment. They might create long term employment with better working conditions on a bigger scale in an underdeveloped region for the general public or employment for a very specific target group such as blind or deaf.

Type C social businesses are focussing creating a social impact on the suppliers most often self employed producers of raw materials or trading goods. In the context of Nepal, those are most often small scale farmers lacking technical knowledge, access to the market or management skills.

Type D and E are less directly related with the social problem. In Type D social business the main drive is to protect the environment. The group of beneficiary is therefore not so clear and the impact the organization has less tangible as many environmental issues occur around public goods and the positive or negative impact often can't be traced back to a single organization.

Type E social businesses are dealing with social problems (or target beneficiaries), which cannot be directly involved in the business process: profit from the business activities is used for funding social activities².

Starting from the understanding that social businesses is a highly ambiguous concept the next chapter shall make an institutional analysis of the context in Nepal. What shapes organizations set up a social business, in which form do they appear and what is their output.

3 A Brief Institutional Analysis of Social Business in Nepal

To answer the question on how institutions shape innovation Hollingsworth (2002) has reviewed existing literature and research and finally developed a five level topology, which is show in Figure 2.

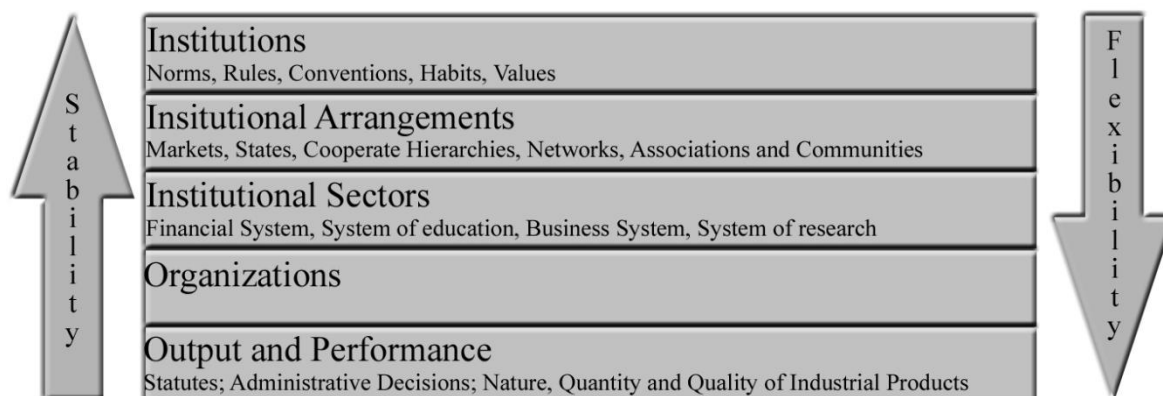


Figure 2 Levels of Institutional Analysis (own design based on Hollingsworth)

Norms, Rules, Conventions, Habits and Values form the first tier he calls institutions, which is the most stable and long lasting element of all. Those further more constitute the basic institutional arrangement, which can have different appearance throughout space and time (i.e. regulatory state, welfare state, authoritarian state) and are shaping furthermore the institutional sectors. Those in turn influence the form of organizations emerging which eventually produce the output, which is the most flexible level, which can easiest adapt to a changed environment.

If we raise the question, why or why not a certain form of organization such as social business emerges in a society or not we need to look at the constitutional settings, such as applicable norms, institutional arrangements and the influential sectors.

² For example a restaurant in a touristic city which is used to cross-finance a school in rural Nepal.

3.1 Level 1 – Norms, Habits and Values

In his book *Predictable Irrationality* Ariely dedicates one chapter on social norms and market norms. He describes social norms the norms which are “wrapped up in our social nature and our need for community” and calls them the „warm and fuzzy” way we ask for a favour and not involving any expectations of reciprocity. On the other side there are the market norms, which are sharp edged and normally based on the idea “you get what you pay for”. Various experiments have shown that if people do something for the good cause they put more effort than if there was a market incentive in form of a payment. Yet, once social norms and market norms collide in general the market norm will be dominant and supersede the social norm. He finally concludes with the finding, that once a social norm has been replaced by a market norm it is hard to come back to the social norm. (Ariely, 2008: 96).

The late opening of Nepal towards an economic development according to a western idea of economy caused only a recent introduction of many parts of the society to a capitalist economic value system. Therefore it has only been a few decades that many of the existing social norms have been replaced by market norms³ and there is evidence, that many Nepali (and probably also many other nationalities including development workers in Nepal) consider economization the way to modernization.

Running a social business is therefore an ongoing tightrope walk between two worlds and requires a more sophisticated management of relations and vision setting and the stamina to be outside of the regular categories of NGOs vs. Business.

3.2 Level 2 – Institutional Arrangements

On the second level Hollingsworth identified six forms of institutional arrangements⁴: the market, the hierarchies, the state, the communities, the networks and the associations. Among them the state has the special role to codify and enforce rules for transactions within the market as well as between the various institutional arrangements.

The lack of according legislation, executive and jurisdiction in Nepal reflects in an accordingly negative behaviour of businesses⁵. Regulations like the ban for plastic bags or the prohibition of child labour are not enforced by the executive powers. Therefore hierarchies (organizations) obeying the rules get normally ‘punished’ when entering the market competition, as they have higher costs but still need to compete with other firms not complying with the law.

Costa (2010) warns in her book *The Watchman’s Rattle* about perils of the five supermeme’s which affect our behaviour away from a further evolution of mankind towards a collapse of our species. One of these supermemes is what she calls economization of a society. She describes the

³ For example food security which has in earlier days been organized through a community storehouse filled by everybody according to their capability. Once a family was in need they could take from this storehouse. Nowadays modern food aid brings subsidized food and giving them away in exchange of food vouchers or subsidized prices has made food security underlying the market norms.

⁴ For a typology aligning those institutional sectors along the range of self-interest vs. social orientation and horizontal vs. vertical power distribution see Annex 2.

⁵ A baseline study done by NBI in 2013 showed, that more than 52 % of the businesses feel very serious challenges in conducting their businesses ethically. (NBI, 2013)

phenomenon that strategies which worked in commerce are more and more applied to other aspects of our live. Speaking in institutional arrangements this would mean that the institutional arrangement market is gaining more and more dominance pushing aside communities other arrangements such as communities.

Institutional arrangements are as per Hollingsworth also rather sluggish, so that this trend will still be existent for a while. In this setting social business carries the potential to mediate better between arrangements as it speaks the language of the market as well as of the communities.

3.3 Level 3 – Institutional Sectors

The type of social business (see above), the business field the social business is working and finally the social issue it is dedicated to constitutes the institutional sectors a social business operates, so that we can find social businesses in a variety of sectors. Even though there is no primary data available on the numbers of social businesses in the different sectors there are a few sectors which influence every social business such as the finance sector, (entrepreneurial) education sector or the governmental framework for setting up new legal entities. Even though financing can also be an obstacle for some projects all of them have to go through legal registration and therefore confronted with some very hands on issues.

For better recognition as a distinctive form of organization, several countries have adapted an own legal status. In 2006 the government of Nepal amended the company act and included a provision under chapter 19 for a “company not distributing profits”. This legal form allows the organization to engage in all kind of income generating activities (in contrary to the legal form of NGOs), while ensuring a social responsible behaviour.

Nevertheless, while implementing such companies – especially in remote areas of Nepal - there are some bureaucratic hurdles. Firstly, the registration process as well as the process of reporting salaries and other data is totally centralized (as is it for the legal form of private limited).

The initial needed capital has to be provided in form of grants, donations or non-refundable membership fees. This does on the one hand not allow for the idea of the ‘recycled donation dollar’⁶ and prohibits on the other hand the idea of ownership of the company. This prevents investment, ownership as well as the legal transfer of the business i.e. within the family or to other members of the community.

In a similar way would a brief analysis of the other sectors would show a similar picture: some first approaches have been made to provide a platform for social business, yet this new arrangements are rather in a very early phase and do not yet for a fertile and well harmonized in eco-system for social businesses.

⁶ One of the major arguments Prof. Yunus brings up, why Social Businesses have a clear advantage to NGOs, is that they are able to recycle invested dollars. No matter how long it takes but once the business reaches break-even, the invested money can be given back to the investors and therefore reused for creating a new Social Business. Profit earned after refunding, will stay within the business and used for improving and expanding its social impact.

3.4 Level 4– Organizations and outputs

Having revisited some critical constraints underlying the establishment of a new social business, this last chapter shall provide not more than a brief overview on the current scene in Nepal.

One of the most comprehensive databases on social businesses in Nepal was most probably collected by Change Fusion, which was running the Surya Nepal Social Entrepreneurship Award for 3 years. Based on their data a sample of 49 social businesses has been reviewed and the results are shown in Figure 3.

Row Labels	Within Kathmandu Valley	Outside Kathmandu Valley	Total
Type A – Customer oriented (Low Income Client Model)	2	1	3
Type A – Customer oriented (Fee for Service Model)	5	2	7
Type B - Employment Model	15	7	22
Type C – Supplier Entrepreneur Support Model	4	2	6
Type D - Environmental Model	2	4	6
Type E - Service Subsidization Model	3	2	5
Grand Total	31	18	49

Figure 3 - Social businesses of Nepal according to their types and regions

A clear majority of social businesses are working towards employment generation and most of them are doing so in the cities. If we look at all client oriented types basically a fifth of all organizations are trying to create its impact through its product. A closer look at this dataset the most of the activity is taking place in the relatively better developed city area⁷; only a minority of the social business seems to target low income clients in the rural areas of Nepal.

What seems on the first glimpse like a negligible fact is indeed part of a core problem. As Sen (2000) has argued the primary reason of markets for development lies not in its results, but in the mere fact of participating in it. As Patsch (forthcoming) shows in her paper, the rural areas of Nepal are facing a very different set of problems caused among other fact by its geographic situation which makes it totally unattractive for traditional business to invest in factories there or target this population as a market. Yet areas such as Jumla already came in the focus of purchasing agents who yearly buy up the various agricultural products creating a kind of paradox in which due to the absence of vegetables and fruits in available in the market leaves more than 50 % of the children malnourished.

Many organizations have basically the goodwill to positively contribute to their society and environment, yet are not able to fully have an integrated concept.

⁷ The term Kathmandu Valley refers to a bowl shaped valley in the middle of the hilly area of Nepal, which is made up of the districts Kathmandu, Bhaktapur and Lalitpur over an area of around 570 km². All three cities are the best developed area in Nepal.

3.5 Level 5– Output and Performance

On this last level of analysis we need to ask, what is the output of a social business? Considering that a social business primary exists for solving a social problem, this level of analysis has to raise the question if a solution for the initial problem has been achieved rather than how much products or services have been produced.

Even for Type A social businesses there can be a slight difference between the both. Imagine a small factory in the middle of the hills producing fortified pulp food to reduce malnutrition among infants. The sales volume would not say much about the success of the project. Rather the organizations will need to stay in close contact with the families to understand if their approach works or not.

Also for Type B social business the measurement of performance has various dimensions: Is the employment created in urban centres or in rural areas? Does it provide permanent jobs with a yearly predictable salary instead of the often precarious situations of day labour? Does it provide jobs for people who have trouble entering the job market otherwise?

We see that on this level the typology of social business plays an even more important role, as it provides the guidance on what are the essential outputs of the social business in relation to its mission.

Hollingsworth described the output and performance is the most flexible one, when it comes to implementation of innovation. Yet a sole change on the output and performance level might not be enough to turn a traditional business into a social business rather I would claim it would need to undergo accept fundamental changes in its organizational structure. That's why social business start-ups seem the more sound way to eventually creating social output and performance.

4 Conclusion

Much of the data provided here and much case studies presented would require more critical scrutiny and ground research to come to more reliable statements. Yet the evidence we get from this short analysis indicates that social business - in form of the idea of a business with a social objective rather than an organization following strictly the seven principles - has found its way to Nepal on an organizational level. These social businesses are more defined by a pioneer mentality as only limited supportive structures can be found on the third level of analysis: the institutional sectors.

This degree of novelty makes being a social business start-up at the moment less attractive and following the idea behind the institutions it would take quite some more time and considerable efforts before a more viable environment for social business will arise in Nepal. Whether such a movement will arise or not depends on if the social businesses promoters of Nepal manage to unite their voice towards a better environment as well as of course further international development of the capitalist economy and the boundaries as well as possibilities it implies on Nepal.

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Annex 1 – Fundamental

Fundamental Models	Relation: beneficiary - social business	Correlates with Social Type	Core activities towards the Target Population
Entrepreneur Support Model	Client (entrepreneur)	(C)	Providing services to self employed individuals or small firms
Market-Linkage Model	Client (entrepreneur)	C	Providing information about the market to buyers and sellers and help thereby to connect those actors directly.
Fee-For-Service Model	Client (in s individual role)	A	Commercializing the social service and selling it to target population (i.e. tuition classes, associations with membership fees)
Low-Income Client as Market Model⁸	Client (in a individual role)	A	Providing goods and services to the low-income groups considering their special needs for price, distribution or product features.
Market Intermediary Model	Supplier	C	Buying products from the target population and act as an intermediary to sell those products to a market.
Employment Model	Employees	B	Providing employment to the target population
Cooperative Model	Mixed but mainly Clients and Suppliers.		The clients are firstly members of the cooperative and benefit in a democratic way from the variety of benefits of the cooperative. They can also be clients, producers, employment or suppliers at the same time
Service Subsidization Model	Business-wise unrelated beneficiary.	D	Create profit from selling products or services to an external market and use the income generated to run social programs.
Organizational Support Model	Business-wise unrelated beneficiary	-	Creates profit from selling products or services from one organization to finance a second organization which provides social programs.

Table 1 Fundamental Models of Social Enterprises based on Alter (2015)

⁸ Even though this model has the potential to be financially sustainable, Alter also points out that “due to the low incomes of the target population [] achieving financial viability can be challenging.” Therefore this model often comes as an social enterprise integrated in a traditional, profitable business.

5 Annex 2 – Typology of Institutional Arrangements

