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# A Positive Theory of Social Entrepreneurship

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**Abstract** I propose a theory aimed at advancing scholarly research in social entrepreneurship. By highlighting the key trade-off between value creation and value capture and explaining when situations of simultaneous market and government failure may arise, I suggest that social entrepreneurship is the pursuit of sustainable solutions to neglected problems with positive externalities. I further discuss the situations in which problems with externalities are likely to be neglected and derive the central goal and logic of action of social entrepreneurs, in contrast to commercial entrepreneurs. Overall, this article provides a conceptual framework that allows understanding the growing phenomena of social entrepreneurship and its role in the functioning of modern society.

**Keywords** Social entrepreneurship · Theory development · Market failure · Capitalism · Externalities · Empowerment · Sustainable solutions

## The Need for Theories of Social Entrepreneurship

Social entrepreneurship, commonly defined as "entrepreneurial activity with an embedded social purpose" (Austin et al. 2006), has become an important economic phenomenon at a global scale (Dacin et al. 2010; Mair and Marti 2006; Zahra et al. 2008). Some striking social entrepreneurship innovations originate from developing countries and involve the deployment of new business models that address basic human needs (Seelos and Mair 2005), such as the provision of low-cost cataract surgeries to cure blindness or the deployment of sanitation systems in rural villages (Elkington and Hartigan 2008). Yet, social entrepreneurship is a vibrant phenomenon in developed countries as well. For example, according to the estimates of the Global Entrepreneurship Monitor 2005 survey, 1.2 M people in the UK (representing 3.2 % of the working age population) are social entrepreneurs (defined in the survey as being involved in founding and running a social-mission organization younger than 42 months). Given that the comparable number for commercial entrepreneurship is 6.2 %, these data raises the intriguing possibility that social entrepreneurship may become almost as important a phenomenon as commercial entrepreneurship (Harding 2006).

Although social entrepreneurs usually start with small initiatives, they often target problems that have a local expression but global relevance, such as access to water, promoting small-business creation, re-integration of individuals into the work-force or waste management. The innovative solutions that social entrepreneurs validate in their local context often get replicated in other geographies and can spun global industries (Zahra et al. 2008). An example is the growth of the microfinance industry throughout the world (Seelos and Mair 2005) which now reaches more than 100 million clients worldwide (Rhyne 2010). Social entrepreneurship is thus having profound implications in the economic system: creating new industries, validating new business models, and re-directing resources to neglected societal problems.

Despite some skepticism about the ability of social entrepreneurs to solve large-scale societal problems (Sud et al. 2009), these developments have sparked a growing academic interest for this new domain (Dacin and Dacin 2011). Practitioner-oriented research and several books focused on social entrepreneurship have been published in the last few years (Dees et al. 2001; Elkington and Hartigan

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2008; Nichols 2006). Business schools which, with a few exceptions (Dees 2001), had largely ignored this phenomenon have been joining the field by creating academic centers and developing new courses (Mair and Marti 2006), a trend that accelerated at the start of this decade. Yet, despite this increasing academic interest, the management field lacks a conceptual understanding of the economic role and logic of action of social entrepreneurs (Dacin et al. 2010). Definitions abound—a recent paper reviewed 20 definitions of social entrepreneurship (Zahra et al. 2009) while another listed 37 definitions (Dacin et al. 2010)—but these were mostly driven by practice rather than theory (Mair and Marti 2006). Mainstream approaches typically (and tautologically) define social entrepreneurs as entrepreneurs with a social mission (Dees 2001; Martin and Osberg 2007) and consider social entrepreneurship as entrepreneurial activity with an embedded social purpose (Austin et al. 2006). Definitions are often derived from the combination of these two concepts—entrepreneurship and social mission (Mair and Marti 2006; Martin and Osberg 2007). Social entrepreneurship has also been called the simultaneous pursuit of economic, social, and environmental goals by enterprising ventures (Haugh 2007). One approach offers a more idealized view of social entrepreneurs as change agents in the social sector (Dees 2001). This approach contrasts with more pragmatic definitions that see social entrepreneurship as the generation of earned income by ventures in the pursuit of social outcomes (Boschee 2001).

The field of social entrepreneurship has thus become a large tent (Martin and Osberg 2007) where distinct activities find a home under a broad umbrella of "activities and processes to enhance social wealth" (Zahra et al. 2009) or "entrepreneurship with a social purpose" (Austin et al. 2006). As a consequence, the concept of social entrepreneurship is poorly defined and its boundaries with other fields of study remain fuzzy (Dacin and Dacin 2011; Mair and Marti 2006). Some authors consider this inclusive approach a beneficial situation for the development of the scholarly field of social entrepreneurship (Nichols and Young 2008). They suggest that social entrepreneurship is connected with and may enrich more established fields of inquiry such as structuration theory, institutional entrepreneurship or social movements (Mair and Marti 2006), and also cultural entrepreneurship and commercial entrepreneurship (Dacin et al. 2010). They also suggest that we do not need a new theory (Dacin et al. 2010) since social entrepreneurship should be seen as a context to study the broader phenomena of entrepreneurship.

In contrast to this inclusive approach, I argue that, at such a pre-paradigm stage of development (Kuhn 1962), the field is better served if knowledge about social entrepreneurship is developed though the elaboration of sharper, well-bounded theories that compete for attention and validation (Martin et al., 2007). As a case in point, the history of theory development in organizational studies in the 1970 points to the importance of apparently restrictive theories at inception, such as institutional theory, population ecology, and transaction cost economics, in subsequently shaping the field's development.

Moreover, in the process of knowledge development, a new theory may be necessary if there is an aspect of reality that is not well explained nor conforms to existing theories. In the case of social entrepreneurship, the emergence of a wave of entrepreneurial actors that, in comparison to traditional commercial entrepreneurs, have distinct goals, use different approaches, and focus on different domains of work, begs for theories that can help us explain what we observe and predict outcomes. Yet, social entrepreneurship theory lags far behind its practice (Murphy and Coombes 2009).

In essence, to move the field forward we need well-defined theories (Pfeffer 1993) that clarify what is social entrepreneurship, explain its distinctive role in the economic system, and inform research and practice, competing with other theories for validation and relevance. My goal with this article is to propose one such theory. In particular, I aim to develop a theory that addresses two issues that have plagued prior attempts at theorizing in this domain: tautology and subjectivity.

First, I aim to move away from the tautology of explaining social entrepreneurship by adding the adjective "social" to characterize elements of the definition (e.g., social goal, social mission, social change, and social value). For example, Dacin et al., in their analysis of 37 definitions of social entrepreneurship, find that a common denominator is defining social entrepreneurship as "the primary mission of the social entrepreneur being one of creating social value by providing solutions to social problems"(Dacin and Dacin 2011). Clearly, a rigorous definition of social entrepreneurship should avoid using the word "social."

Second, I aim to develop a positive theory of social entrepreneurship, not a normative one. If we take social entrepreneurship as a context (Dacin et al. 2010), we need to subjectively assign a normative connotation of "social" to some activities and not to others. For example, helping low-income people is social entrepreneurship, helping high-income people is not. Yet, where do we set the income threshold? Or, another example, providing food for low-income people is social entrepreneurship, providing mobile phones is not. However, mobile phones have proven to be a very effective tool for poverty alleviation so discriminating against them would seem counterproductive for achieving a social mission. I aim to develop a positive theory that avoids normative classifications of what is social and what is not. A theory that is useful to describe and predict the reality in which social entrepreneurs operate, a reality that traditional entrepreneurship theory seems ill-suited to describe.

In order to explain the distinctive role and approach of social entrepreneurship, I start by defending a holistic conception of value and proposing that the trade-off between value creation and value capture is a central choice for organizations. Then, I associate a focus on value creation with social entrepreneurship and explain the unique role of social entrepreneurship in the current architecture of the modern economic system. Based on this analysis, I define the distinctive domain of social entrepreneurship as addressing neglected problems with positive externalities. From this argument, I derive the central institutional goal and logic of action in social entrepreneurship. Finally, I discuss the implications of the proposed theory for our understanding of the economic system and for the advancement of the academic field of social entrepreneurship.

## A Holistic Conception of Value

In order to develop a well-bounded theory, I argue that first we need to abandon the traditional distinction between economic and social value that is so often associated with definitions of social entrepreneurship. It is commonly argued that social entrepreneurs are entrepreneurs with a social mission as opposed to a profit-seeking motivation. Their goal is to create social value. For example, Certo and Miller (2008) argue that "Social value has little to do with profits but instead involves the fulfillment of basic and long standing needs such as providing food, water, shelter, education and medical services to those members of society who are in need." This dichotomy between economic and social value poses several problems for theory development. First, all economic value creation is inherently social in the sense that actions that create economic value also improve society's welfare through a better allocation of resources. Second, some may argue that economic value is narrower than social value and only applies to benefits that can be measured monetarily, while social value includes intangible benefits that defy measurement. This argument, however, creates methodological difficulties for a positive theory because its logical implication is the need to develop a theory based on elements that, by definition, are not measurable, making the theory difficult to test empirically. Third, the dichotomy between economic and social value is problematic for theory development because it requires subjective assessments about the domain of social entrepreneurship. What counts as "social" and who is in need of "social help" is inherently a normative judgment. It assumes that there is some metric or set of values that make certain types of value creation "social" and others not. This distinction is thus relative to the observer. A positive theory of social entrepreneurship should not be built on such a basis.

I thus reject the dichotomy between economic and social outcomes. It is more effective for theory development to focus on a generic concept of value, defined in terms of the increase in the utility of society's members. This is consistent with the treatment of the concept of value in economic theory, for which social welfare is defined by the aggregation of individual utility. It is also consistent with more applied notions such as blended value (Emerson 2003). Although this can be considered a restrictive assumption, it allows placing the theory of social entrepreneurship in the mainstream of economic and management thinking. The litmus test will be the extent to which such a theory helps explains a facet of reality not well explained by competing theories. If we assume such a holistic concept of value, what is then the most relevant distinction to explain how social entrepreneurship is different from commercial entrepreneurship? I argue that the central distinction is between *value creation* and *value capture*.

### Value Creation and Value Capture

Value creation from an activity happens when the aggregate utility of society's members increases after accounting for the opportunity cost of all the resources used in that activity. Value capture from an activity happens when the focal actor is able to appropriate a portion of the value created by the activity after accounting for the cost of resources that he/she mobilized (Mizik and Jacobson 2003). This means that value creation is a concept measured at the societal or system level, while value capture is measured at the organizational or unit level. The traditional notion of profit is no more than an estimate of the value captured by an organization.

This distinction between value creation and value capture is becoming a key concept for the field of strategy (Lavie 2007). It is clear that value creation is a necessary condition for sustainable value capture. Activities that allow value capture without value creation will be considered illegitimate and probably quickly outlawed due to their burden to society (examples are Enron profiting from electricity markets based on price manipulations or industrial activities that heavily contaminate the environment). It is also clear that some level of value capture is important to ensure the growth and sustainability of the organizations whose activities create value—this explains, for example, the fast pace of growth of microfinance organizations able to develop a financially viable business model (Rhyne 2010).

Yet, these two dimensions are not perfectly correlated. Some activities that create substantial value for society do not easily allow for value capture because of significant value spillovers due to externalities (Rangan et al. 2006) (for example, the mentoring of recently freed inmates to prevent crime re-incidence). In addition, value may be hard to capture because of the inability to pay of the target customers despite willingness to pay if funds would be available (Seelos and Mair 2005) (for example, curing blindness of low-income populations through a cataract surgery creates substantial value for society but the client cannot pay for the procedure). More striking, some organizational actions increase the potential for value capture in detriment of value creation (for example, a price increase that increases revenues and profits for the organization but lowers the sales level thus reducing total surplus). This suggests that economic actors regularly need to make trade-offs between value creation and value capture.

The importance of these trade-offs are well established in the field of strategy. For example, work on strategic alliances argues that alliance activities by firms have distinct value creation and a value capture mechanisms (Lavie 2007). Work on strategic marketing recognizes that managers, when allocating attention and resources in organizations, have to make trade-offs in terms of the emphasis they place on value creation versus value capture (Mizik and Jacobson 2003). Moreover, these choices have consequences in terms of how the organization is perceived by its stakeholders and valued by the market. For example, share prices increase when firms shift emphasis from value creation to value capture strategies (Mizik and Jacobson 2003).

Given this trade-off, I argue that organizations need to be clear about their predominant focus being value creation or value capture. This choice is so central to the organizational identity that any perceived shift or ambiguity can cause upheaval on stakeholders and may lead to a loss of legitimacy. For example, the Mexican Bank Compartamos operated for many years as a typical microfinance institution—maximizing on value creation by lending to the poor and charging an interest rate that allowed it to cover costs and reinvest in growth (Rosenberg 2007). In the 1990s, the managers of the bank were forced to significantly raise their interest rates to cover their costs during a period of high inflation in Mexico. After the inflation suddenly came down, they found that their business model was highly profitable and decided to maximize profits to increase their growth potential. So, instead of lowering their rates, they kept them at close to 80 % and re-invested the profits in an aggressive growth strategy with a view for a public offering of shares (IPO). The managers and initial investors cashed out in the IPO conducted in 2007 with extremely high rates of return on their initial investment. The bank was valued at more than 1 billion US$ given the level of growth and future profits promised. Naturally, the new shareholders will expect and demand a continuation of this value capture strategy. As a result, the bank lost legitimacy in the microfinance field because of its perceived shift from value creation to value capture (Pache and Santos 2010). Microfinance opinion leaders, such as Muhammad Yunus the founder of Grameen Bank and Nobel Prize winner, challenged Compartamos actions arguing that Microfinance risked losing its soul. Compartamos leaders had to publish a letter in defense of their actions, arguing that a strategy of value capture was the most effective approach to develop the microfinance industry (The Economist 2008).

This example suggests that maximizing both value creation and value capture in the same organizational unit is difficult. Although value creation and value capture can be sometimes aligned, trade-offs will eventually emerge. A central argument for the theory proposed in this article is that organizations need to clarify if their overarching goal is value creation or value capture and be clear and consistent in communicating their choice. This choice then has important consequences for organizational actions. For example, an organization that is predominantly focused on value creation would typically set the price of its service at the point that would maximize the utility for its users and clients (subject to the organization's sustainability). In contrast, as the Compartamos example illustrates, an organization focused on value capture would set the price of its product at the point that maximizes its expected profit potential. More importantly, the value creation versus capture trade-off is central to the choice of the activities to be performed by the organization (and not just their price level or quantity). For example, a pharmaceutical company focused on value capture would not invest in vaccines for diseases that plague developing countries due to the lack of ability to pay by its potential clients. In contrast, a pharmaceutical company focused on value creation would have a motivation to invest in that activity, independent of the amount of value that it would be able to capture, given the strong and measurable impact for society of disease eradication. An illustration is OneWorld Health, a not-for profit pharmaceutical firm launched in the US in 2000, which is considered a good example of social entrepreneurship (Seelos and Mair 2005). The value creation focus of OneWorld Health allowed the firm to engage with stakeholders in novel ways and re-design the pharmaceutical value chain to deliver effective drugs to fight the most prevalent (and often neglected) diseases in developing countries.

These arguments suggest that organizations (or at least their sub-units) need to be clear about their central goal being value capture or value creation. In most situations, organizations will maximize one of the dimensions and satisfice on the other dimension. For-profit corporations usually have a clear goal of maximizing value capture and satisficing on value creation by following legal requirements and engaging in socially responsible actions. Social-mission organizations usually maximize on value creation and satisfice on value capture by aiming to capture just enough value to sustain operations and re-invest in growth.

Sometimes, organizations may adopt both approaches but they usually do so in different organizational units. For example, Bridges Ventures is a UK venture capital firm that was set up in 2002 to invest in economically deprived areas of the UK. It raised a fund that set a high standard of satisficing on value creation by choosing geographical areas for investment where entrepreneurial activity would have a strong societal impact and then set the goal of maximizing the financial returns to investors within that constraint. Yet, its managers realized that many opportunities for value creation through social impact investments were not explored because of their mandate to maximize financial returns. Thus, in 2008, Bridges Ventures created a social entrepreneurs' fund that satisfices on financial returns by aiming to ensure a rate of return equivalent to bank deposits, but then makes investments in social entrepreneurship initiatives with the goal of maximizing social impact. Naturally this fund attracted a different set of investors who were primarily motivated by social impact not financial returns.

In contrast to these arguments, proponents of concepts such as the triple bottom line (social, financial, and environmental) call for organizations to develop strategies that maximize on different variables (Elkington 1998). Although in some instances it may be possible to temporarily develop win–win scenarios and combine goals, conflicts will inevitably arise when the trade-offs between value creation and value capture surfaces. An example is Grameen Phone, a partnership between Telenor (a Norwegian telecom firm) and Grameen Telecom (the telecom subsidiary of Grameen Bank founded by Yunus). The goal of Grameen Phone, established in 1996, was to deploy low-cost mobile phone access in Bangladesh. The astounding success of this initiative made it the largest and most profitable telecom company in Bangladesh and a significant growth driver in Telenor's mature portfolio of businesses. This success led to a clash of interests between the partners as Telenor later reneged on an earlier promise (made by the former CEO) to cede majority ownership of the joint-venture to Grameen Telecom so that the social venture could share the value created with the users. Telenor executives argued that its promise was just "an intention," not a binding contract, and that its current strategy required keeping majority control of all foreign subsidiaries. Yunus threatened to file a lawsuit against Telenor if the situation was not resolved. He argued that "the agenda of Telenor to maximize returns for the benefit of its owners is...in conflict with the social and non-profit agenda of Grameen Telecom" (Yunus 2008).

In contrast to the problems plaguing the Grameen Phone partnership, the later partnership between Grameen and the French dairy multinational Danone has been much less contentious (Yunus 2007). The goal of Grameen Danone is to reduce malnutrition of Bangladeshi children through the local production and sale of low-cost yoghurts enriched with vitamins. Danone's CEO created a separate governance structure called Danone Communities for managing such partnerships and made clear that Grameen Danone is an autonomous social business that needs to be financially sustainable (thus satisficing on value capture) but has the goal of maximizing on value creation for society. To secure this arrangement for the long term, Danone's leadership cannot change the partnership structure at a later date.

In summary, I argue that organizational entities will have a predominant focus on either value creation or value capture. Moreover, any change in the main focus or any ambiguity about the organization's positioning on this issue will be identity challenging (Tripsas 2009). This happens due to the embeddedness of organizations in a web of relations and institutional expectations that are associated with either value creation or value capture.

Building on this central dichotomy, I argue that what distinguishes social entrepreneurship from commercial entrepreneurship is a predominant focus on value creation as opposed to value capture. Although many entrepreneurs, when launching their ventures, may be ambivalent between value creation and capture, quickly they need to make choices about whom they bring on board as partners and investors. Often, they build organizations and engage other stakeholders (co-founders and employees who receive shares, investors such as business angels and venture capitalists) who wish to capture value to compensate for their resource commitments. Alternatively they may engage with foundations and volunteers, who will require a focus on value creation as the dominant goal. So, even if founders are driven equally by value creation and capture, their early choices will lead to a specific path for the organization. For example, when Jeff Skoll joined Pierre Omidyar as co-founder of eBay, the venture had a good balance between value creation and value capture given the focus of the founders on building a fair auction system by empowering its community of users. For example, payments to eBay for using the platform were not enforceable as they depended on the good will of users to send checks by mail. Yet, once the founders accepted venture capital to speed up growth and the investors brought Meg Whitman on board as CEO, eBay clearly moved into a path of focusing on value capture. The new executives raised the fees, segmented users, and tried to control the community. The two founders then disengaged from eBay. Interestingly, they later donated most of the wealth they made with eBay to philanthropic activities (including endowing the Skoll Foundation to support the growth of social entrepreneurship throughout the world and the Omidyar Network to support microfinance investments). This suggests that although individual may have multiple goals, organizations need clarity of purpose in order to engage with their institutional environment in coherent ways. They may need to choose either value creation or value capture as their dominant focus.

Naturally, what matters for a theory of entrepreneurship is the intended goal of the economic actors, not their eventual success or failure in creating and/or capturing value, which can only be known ex-post and depends on the quality of execution of organizational activities. Overall, my argument is that activities perceived as having a high potential for value creation but a low potential for value capture are a natural domain of action for economic actors predominantly driven by value creation, such as social entrepreneurs.

Interestingly, these ideas relate to the arguments of Ghoshal and Moran (2005) who reject the focus on value capture that exists in economics and strategy theories and call for value creation to be the "raison d'etre" of the modern corporation. Although I agree on the trade-off between value creation and capture, the approach I adopt in this article is positive not normative. Instead of calling for all corporations to focus on value creation, I acknowledge that different behavioral motivations may lead to distinct organizational emphasis within the value creation and capture trade-off. This allows developing a theory of social entrepreneurship that is rooted in established paradigms in economic organization and does not need to rely on conventional dichotomies of economic versus social. Next, I discuss the role of social entrepreneurship in the context of the economic system.

## The Architecture of the Economic System

I argued in the introduction that the management field lacks a conceptual foundation that can clarify the distinctive role of social entrepreneurship in society and explain the unique attributes of a social entrepreneurship approach when compared to commercial entrepreneurship (Austin et al. 2006). In the modern economic system, characterized by market-based capitalism with a varying level of government sponsored services and an active social sector, what is the role and distinctive domain of social entrepreneurship? To answer this question, we need to probe deeper into the architecture of the economic system.

Economic theory suggests that, in perfect market conditions,[1] economic agents pursuing their own self-interest (usually narrowly defined as profit maximization but associated here with the broader concept of value capture) will lead the economy to an outcome in which resources are put to the best possible use and individuals will consume the services that they most value. This outcome will in turn maximize welfare. This is the fundamental insight of the invisible hand, initially suggested by Adam Smith in the 18th century (Smith 1922) and later demonstrated by neo-classic economists (under somewhat stringent assumptions).

Naturally, economies are not static. New needs, new technologies, and new information arise, enabling new opportunities for improvement in the organization of resources and delivery of goods and services. However, profit-oriented companies often invest resources and skills in becoming efficient in certain areas of activity. They may then miss new opportunities or, even if they identify them, they may not have incentives to invest in new resources, structures, or services given the underlying ambiguity of new areas compared to the clarity of their current business (Santos and Eisenhardt 2009). Thus, managers and their corporations may become locked into increasingly erroneous views of the world (Hodgkinson 1997), their core capabilities become core rigidities (Leonard-Barton 1992), and the business model that made them successful may no longer constitute a good fit with the environment (Zott and Amit 2008).

It thus falls upon commercial entrepreneurs to pursue new opportunities for value capture, often creating a new market in the process (Santos and Eisenhardt 2009) or developing an improved service or changing operating procedures to reduce the costs of activities. Competition from entrepreneurs then forces established corporations to either adapt their business processes to remain competitive or risk losing their ability to compete. This often means adopting the innovations introduced by entrepreneurs or acquiring the innovative firms (Markides and Gerosky 2005). Commercial entrepreneurship is thus the dynamic and distributed mechanism that keeps economies evolving toward a state in which resources are allocated and organized in the best way possible to benefit society (Schumpeter 1934).

Yet, economic activity cannot happen in an institutional vacuum. There is the need for a central actor, such as the

[1] Which in its most extreme form requires perfect competition (no increasing returns to scale, multiple buyers and sellers), complete information available to all economic actors, and no transaction costs or externalities.

government and its institutions, to establish the legal infrastructure of the system and enforce it. This infrastructure includes elements such as property rights and the rule of law. Moreover, in their pursuit of value capture, corporations may often push their mandate to maximize profits beyond what is socially acceptable, abusing their dominant position or developing anti-competitive tactics that reduce the value for society. Thus, the government also performs a crucial regulatory function, setting the legal and monitoring framework that guarantees that competitive market conditions are maintained.

Although this type of self-interested competition in regulated market conditions may be an optimal system from an economic efficiency point of view, this system may not lead to equitable economic outcomes since differences in initial resource endowments and capabilities often generate inequalities in the later distribution of resources and welfare. To address this, governments often assume a re-distributive function, through the tax system and social coverage, to try to ensure to every individual in society a minimum accepted level of individual welfare. Yet, governments often do not have the means or capabilities to perform this re-distribution function, particularly when action is needed at a local level. The visible hand of the government is blunt and favors general solutions not customized actions. Here enter charitable organizations and NGOs, which are groups of citizens concerned about a particular social inequality who create an organization that re-distributes resources to reduce that inequality or offer services for free or at low cost to disadvantaged populations. Charities usually source funds from governments, philanthropic organizations such as foundations, and wealthy individuals to pursue their mission. Charities thus constitute the dynamic and distributed mechanism that makes economies move toward a more just distribution of resources and economic outcomes.

Unfortunately, the appealing architecture of the economic system outlined above is weakened by the presence of externalities. Externalities exist when economic activity creates an impact (or value spillover) that lies beyond the objective function of the agents developing the activity (Rangan et al. 2006). When this happens, the decisions of self-interested actors are no longer optimal for society since actors are ignoring in their decisions the positive or negative impact of their activities on others. In the case of negative externalities, the consequences are usually the adoption of harmful practices for society (e.g., dumping toxic waste) or the over-production or over-consumption of activities that bring negative consequences (e.g., excessive car usage leading to road congestion). In the case of positive externalities, the consequence is usually the under-provision of goods, such as education or vaccination, that create value for society much beyond the value created to the recipient of these goods. To achieve an optimal economic outcome, these externalities need to be internalized by economic actors in their decisions. One can argue that the trend for corporate social responsibility represents the duty of profit-oriented corporations in accounting for the full cost of their activities to society, even beyond existing legal requirements. However, self-regulation by corporations may not be fully effective given their focus on value capture.

This gives Governments a key role in dealing with externalities. There are three main government mechanisms to correct for negative externalities—regulation, taxation, and market creation. Either the Government introduces regulations forbidding the behaviors that lead to negative externalities (e.g., recycling directives; law forbidding production and consumption of narcotics) or introduces incentives to reduce activities with negative externalities (e.g., gasoline and tobacco taxes) or creates market-based mechanisms that price these negative externalities and incorporate them in the agents' decisions (e.g., the carbon-emission trading system). However, if the market failure is caused by positive externalities, it leads to under-provision or under-consumption of beneficial goods (Rangan et al. 2006). Governments again have a key role to play in correcting these market failures. They may either decide to provide those services directly through governmental organizations when they are considered public goods (which are goods that have the characteristics of being non-rival and non-excludable in consumption, such as national defense) and/or governments can create a system of public subsidies that generates an incentive for private economic actors to provide these services (e.g., education vouchers; R&D incentives; subsidy for renewable energy).

Yet, governments have multiple roles and often scarce resources, which suggests that some externalities are likely to be neglected. What is the distributed mechanism that ensures that externalities are continuously being identified and internalized in the economic system? I suggest that this mechanism is social entrepreneurship and that addressing neglected problems with positive externalities is the distinctive domain of social entrepreneurship. I elaborate this argument next.

## The Distinctive Domain of Social Entrepreneurship

As I argued earlier, a central difference between commercial entrepreneurship and social entrepreneurship is that social entrepreneurs are driven primarily by a motivation to create value for society, not to capture value. What legal form an entrepreneurial organization actually adopts (profit vs. non-profit status) and whether entrepreneurs eventually capture value through their activities or not (their venture may fail or their perception about the potential for value capture may have been wrong) is less relevant for a definition of social entrepreneurship than the agents' motivations for economic action.

I also assume that, in many activities with a perceived potential for value capture, commercial entrepreneurship is a more effective mechanism for action than social entrepreneurship due to the strength of market-based incentives in capitalist economies. For example, let us imagine that an activity that has a potential for value capture starts to be performed simultaneously by a social entrepreneur and by a commercial entrepreneur. Let us assume also that both entrepreneurs are equally effective at developing and validating a new solution for the problem they are addressing. After the initial validation, commercial entrepreneurs are more likely to be able to acquire the resources needed for growth (skilled employees looking for a high salary, partners looking for an equity revenue share, investors looking for a return on their resource commitments, etc.). They will then be able to scale their solution faster than social entrepreneurs, eventually displacing them over the long term. Thus, commercial entrepreneurship may crowd-out social entrepreneurship in capitalist-driven societies or push them to segments of works or clients where markets do not perform well.

So the key question becomes: in which situations do commercial entrepreneurs fail to act and social entrepreneurs can play a role? The answer is in areas with strong externalities, particularly positive externalities, where the potential for value capture is lower than the potential for value creation because the benefits for society of the activity go much beyond the benefits accrued to the entrepreneurs.

These market failures, however, should be tackled by governments since addressing areas of externalities is one of governments' central roles. As explained above, if there is a wide societal perception of the positive externality, effective governments will act by either provisioning the activity themselves or creating public subsidies for the private provision of these activities, either through for-profit actors or through established social sector organizations. This is the case, for example, of the widespread government support for renewable energy production in most European countries or the subsidies for the social integration of long-term unemployed in France. However, in some situations, governments and society may not fully realize the extent of positive externalities in a certain domain. For example, the positive externalities involved with renewable energy production in terms of reducing climate change were invisible a decade ago and still questioned today. Thus, governments often do not have enough knowledge to act, even when they have the resources and motivation to do so. Profit-oriented entrepreneurs, even if they perceive the externalities, will not act on them given the low likelihood of capturing value. It then falls to social entrepreneurs to tackle those neglected problems with positive externalities by providing a solution to them, while alerting society's members to the importance of these problems and the associated value spillovers, so that they can be accounted for in future actions. This is the distinctive domain of social entrepreneurship.

**Proposition 1** The distinctive domain of action of social entrepreneurship is addressing neglected problems in society involving positive externalities.

A micro and a macro examples illustrate this proposition. The micro example is the case of Unis-Cité, a French social enterprise founded in 1995 with the purpose of creating a civic service opportunity for young French people (Pache 2002). The program brought together youngsters from different origins to perform volunteer team work for a period of 1 year in different social projects and programs. Although young French people would benefit in skills and knowledge from this experience, and develop a stronger and healthier understanding of their role as citizens, they would not be likely to pay for this opportunity. Instead, many required a stipend to ensure a living wage for the duration of their volunteer service. However, the organizations offering these projects did not have the ability to pay this cost, even if they saw that the service would create value to them. This led the field of civic service to be neglected by commercial entrepreneurs and also by the government. The government did not even define a legal status for this type of volunteer work, let alone subsidize it. So why would social entrepreneurs develop an offering in this area? The argument was based on a positive externality benefiting society. Given the high unemployment among the youth and the widening societal divisions across religion, race, and residence area (suburbs vs. cities; White youngsters vs. African emigrants' children), the social entrepreneurs argued that such civic service program would create a sense of cohesion among the youth that would greatly benefit French society.

The social entrepreneurs developed a business model, found support among corporate foundations and local governments, and conducted a small scale pilot in Paris in 1998. This pilot was then extended to other French cities in the subsequent years. The value of the initiative was validated by several impact assessments. However, funding for the scaling-up process was difficult, and the French government was not making any progress in the creation of a legal framework. Yet, in 2006, French youth from the suburbs revolted against society and provoked widespread riots across France. The government suddenly realized the importance of the problem of youth integration. They also realized the value of the positive externalities generated by a civic service program of the kind proposed by Unis-Cité. The government then announced, a few months later, a legal framework and sizable funding to develop a large-scale civic service program among the French youth. This led to a significant increase in Unis-Cité's scale in 2007 and to the entrance of other providers into this market, both new ventures and more established social organizations, such as the Red Cross.

This example of a neglected problem with positive externalities being addressed early on by social entrepreneurs and later supported by the government is not an isolated case. Ashoka, the global organization that identifies and supports close to 2000 high-impact social entrepreneurs, claims that over half of the social entrepreneurs in their network influenced national legislation within 5 years of launching their organization (Sen 2007). This suggests that social entrepreneurs' focus on neglected problems with significant positive externalities, develop economic action to demonstrate a solution to address the problem, and then often influence governments to create legislation that legitimates and supports their innovation. This facilitates scaling-up and replication of the innovation, thus reducing the market failure or under-provision in their chosen field. The systematic identification and solution of problems related to neglected positive externalities is the distinctive role of social entrepreneurship in society.

Although the above arguments set out the distinctive domain for social entrepreneurship, a theory of social entrepreneurship should go further and clarify which types of positive externalities are likely to be systematically neglected, even by highly effective governments. I argue that positive externalities whose benefits are both localized and favor less powerful segments of the population are likely to remain neglected by governments. As discussed earlier, the case for government provision is particularly strong in situations where the positive externalities generate goods that are both *non-rival* (the consumption of the good by one individual does not preclude others from consuming—examples are new knowledge or radio broadcasts) and *non-excludable* (once provided there are no mechanisms to prevent individuals from consuming the good—examples are national security or clean air). These are called in economic theory "public goods" and since they benefit society as whole, they are more visible and there are more incentives for governments to intervene.

However, beyond the extreme example of public goods lies a spectrum of goods that generate substantial positive externalities but do not qualify as public goods. These positive externalities may be thus invisible or seem irrelevant to the general public. I argue that this happens in particular when the externalities are localized in the sense that they benefit disproportionally a specific segment of the population, such as isolated populations, racial minorities, or elderly people. In these situations, governments may have a weaker mandate to intervene since they would be using public funds to support a specific group or constituency. An important variable, however, is the power of the affected group. When these localized externalities benefit a powerful segment of the population (defined as having high status, control of resources, ability for collective action, and influence in public opinion) the government has an incentive to act and will be pressured to do so by those society members that care about the issue. Note, for example, the sizable subsidies provided to farmers in most developed countries given the high visibility and collective action capacity of farmers. Let us imagine now that the positive externality accrues mainly to a localized and powerless segment of the population (in powerless we include characteristics such as small in size, low status, low resources, low ability for collective movement, and no influence on public opinion). In these situations the government, faced with many priorities and generally scarce resources, may not notice, is not motivated to, or cannot easily justify to society spending resources and efforts in benefiting a specific segment of the population. These will then become areas of severe under-provision compared to the economic optimal level, representing a government failure, in addition to the existing market failure. Social entrepreneurs, faced with this failure of both markets and governments and feeling passionate about the needs of that particular group or about the characteristics of the problem, will enter this domain and develop a solution to the problem and raise societal awareness about it.

**Proposition 2** Social entrepreneurs are more likely to operate in areas with localized positive externalities that benefit a powerless segment of the population

This proposition is supported by substantial evidence that most activities of social entrepreneurs are directed toward offering services to disadvantaged segments of the population (poor, long-term unemployed, disabled, discriminated, socially excluded, etc.) (Seelos and Mair 2005). However, the proposition also has a very important implication for a theory of social entrepreneurship. Helping disadvantaged segments of the population is *not*, contrary to some definitions (Certo and Miller 2008), the essence of social entrepreneurship. Rather, the defining characteristic of social entrepreneurship is the pursuit of neglected problems with positive externalities. It so happens that the most neglected problems with positive externalities affect disadvantaged populations. This explains why so many social entrepreneurs operate for the benefit of these populations. The logical implication is that efforts to help *advantaged* populations may also constitute social entrepreneurship, as long as it involves addressing problems with positive externalities with a dominant goal of value creation. An example is the development of Wikipedia, the online encyclopedia. This is a service that benefits mostly advantaged populations—literate audiences with access to computers and internet technologies. Yet it represents a good example of how the problems caused by positive externalities in the production of knowledge can be tackled by social entrepreneurs who are able to develop an innovative solution that creates value for society.

Thus, an important implication of the theory proposed in this article is that social entrepreneurs do not need to be defined as "good" or "moral" agents that want to help others. Although helping others is often a motivation for their behavior and an outcome of their activities (Zahra et al. 2009) this is not what primarily defines the role of social entrepreneurs in society. What is distinctive about social entrepreneurs is that they are economic agents who, due to their motivation to create value without concern for the amount they capture, will enter areas of activity where the more severe market and government failures occur. As I argued, these are usually areas with neglected positive externalities affecting disadvantaged populations.

It is important to note that there are many areas in which positive externalities are not neglected but rather appropriately recognized by society's members and subsidized by governments. In that case, those activities can be carried out, depending on their nature, by either commercial-driven or social-mission enterprises, often using well-established methods and solutions. This will no longer constitute social entrepreneurship, in the way that it is being defined in this article as an innovation process in society. For example, running a school in a society where the value of education is well recognized and subsidized by the government is not social entrepreneurship, unless the school uses an innovative approach to either focus on a segment of the population for whom schooling is not yet available (e.g., marginalized youth, children with neglected disabilities) or address a specific and neglected problem with positive externalities (e.g., nutrition, technology, or music education). Effective social entrepreneurs often combine both approaches and develop activities for marginalized populations in areas with neglected positive externalities thus creating a multiplier impact effect. An example is CDI, the Brazilian organization founded by Rodrigo Baggio, an award winning social entrepreneur (Kaiser and Santos 2009). Baggio launched the first information technology school in a slum of Rio de Janeiro in 1995 to fight digital exclusion among the poor Brazilian youth. The goal was to use the seduction of computers to transform marginalized youth into engaged citizens with valued skills, an outcome with substantial positive externalities for society. By 2005, CDI had built a network of close to 1,000 schools across Latin America. Then, the Brazilian government, influenced by CDI's success, Baggio's activism, and the increased awareness in society about the benefits of digital inclusion, launched a national program of digital inclusion. This led to establishment of 6,000 free-access government-based computer centers by 2008, which, alongside the roughly 80,000 Internet cafes that emerged in the private sector, meant that access to computers was no longer a neglected issue in Brazilian society. Social entrepreneurship is thus the catalyst that often gives rise to large-scale solutions that then become centered on markets, government, or the charity sector.

In summary, I used economic and institutional arguments to identify the distinctive domain of action of social entrepreneurship—addressing neglected problems involving neglected positive externalities. This is not to say that social entrepreneurs will never operate outside this domain. They probably will, particularly because the practice-based definition of social entrepreneurship is both broad and somewhat ill-defined. What my arguments demonstrate is that social entrepreneurs are institutional actors that perform a unique role in the economic system, which cannot be substituted in an effective way by any other category of institutional actor. These arguments provide a conceptual basis to develop a theory of social entrepreneurship that is distinct from other theories of entrepreneurship, while still drawing from economic and organizational theory arguments. The next step is to build on this conceptual foundation to understand the unique mode of action of social entrepreneurs and why they are effective in addressing neglected positive externalities. In other words, after having demonstrated the economic usefulness of social entrepreneurs, I will propose a theory of how they operate as economic actors.

## The Distinctive Approach of Social Entrepreneurship

What is unique about the way social entrepreneurs address neglected problems with positive externalities? It is commonly argued that social entrepreneurs develop practical and innovative solutions, given their lack of resources and the scale of the problems they aim to address. However, this is no different from commercial entrepreneurs who, being also resource constrained and aiming to address significant societal problems, need to be innovative and practical, often "creating something from nothing"(Baker and Nelson 2005).

It is also sometimes argued that social entrepreneurs operate in the absence of markets for the problem they aim to address and need to develop new market-based mechanisms. However, commercial entrepreneurs who operate in nascent fields also need to construct new markets around their solution (Santos and Eisenhardt 2009). Moreover, it is not clear why social entrepreneurs would have a preference for market-based mechanisms compared to other type of governance arrangements, such as government provision or public–private partnerships (Rangan et al. 2006). If they are indeed tackling areas of neglected externalities, market-based mechanisms may not be the most efficient form of economic organization to address them.

In order to understand the distinctiveness of social entrepreneurs, we need to go back to my earlier arguments that the key difference between social entrepreneurs compared to commercial entrepreneurs is that they seek opportunities for value creation without regard for the potential for value capture. This predominant focus on value creation has important implications for how social entrepreneurs act. First, social entrepreneurs aim to achieve a *sustainable solution* to the problems they address, as opposed to achieving a *sustainable advantage* for their organization. Second, social entrepreneurs adopt a logic of *empowerment* of others, both inside and outside their organization, as opposed to the more traditional commercial logic of *control*. I discuss next these fundamental distinctions of the social entrepreneurship approach.

### Sustainable Solution not Sustainable Advantage

Organizations driven by value capture are usually concerned with pursuing opportunities for profit and entrenching situations in which their value capture capacity is maintained and, preferably, enhanced over time. In fact, the field of strategy is based upon exploring how firms can achieve a sustainable competitive advantage over rivals (Nickerson et al. 2007). Managers are advised to adopt a firm-centric focus (even when trying to build platforms or eco-systems) and continuously (re)consider the positioning of their organization in the market. Similarly, theories of the entrepreneurial firm place the capture of rents at the center of why some activities are internalized in new ventures (Alvarez and Barney 2004). Thus, commercial entrepreneurs, although aware of the fact that they need to innovate and create value, have to construct a market position that will give them a sustainable advantage since they do not want to see the value they create spill over to other organizations and actors (Santos and Eisenhardt 2009). This notion of sustainable advantage is deeply ingrained in strategic thinking and embedded in our entrepreneurship models. It underlies all theories of strategy, from industry analysis to the resource-based view of the firm and dynamic capabilities approaches.

In contrast, social entrepreneurs are concerned with correcting perceived market and government failures—their focus is achieving *sustainable solutions* instead of achieving sustainable advantage. Sustainable solutions are approaches that either permanently address the root causes of the problem or institutionalize a system that continuously addresses the problem, ideally with minimal intervention from the original innovators. Addressing the root causes of the problem involves developing a solution that eliminates the problem permanently. For example, the development of an effective vaccine for tropical diseases in Africa and its widespread adoption could eradicate a virus completely and eliminate the problem. Institutionalizing a system can either involve the development of a new market-based sector to systematically address the problem (e.g., microfinance) or the establishment of a government sponsored provision model (e.g., free vaccination in public hospitals) or even a combination of the two mechanisms (e.g., public sponsoring of youth volunteer work as described earlier in the Unis-Cité example).

Particularly striking is the development by social entrepreneurs of community-based solutions that initially do not depend on markets or government mechanisms (Peredo and Chrisman 2006). An example is Gram Vikas, a rural development organization in India whose mission is to deploy running water and sanitation systems in rural villages with a mandate of covering 100 % of the households in the villages it works with (Chowdhury and Santos 2011). Gram Vikas developed a solution that involves providing to the villages the technical skills and building materials for water sourcing, piping and sanitation system, while the villagers provide the labor and the commitment that all the households of the village, with no exceptions, agree to install and use running water and sanitation in their house. Moreover, each family needs to invest some of their savings into a village fund that is placed in a bank account. These funds are used to guarantee the maintenance and operation of the sanitation system in perpetuity. Thus, once the system is installed, it is guaranteed to be sustainable. In addition, any surplus generated by this capital is used for community development projects. The Gram Vikas staff supports these projects for 5 years to transfer their skills and approach to the villagers. There are multiple positive spillovers from implementing such a system: a lower level of diseases in the villages, less time spent searching for water, and benefits from building community capacity. Gram Vikas has installed such systems in hundreds of villages and is now transferring its methodology and capabilities to other social organizations.

An implication of these arguments is that social entrepreneurship involves a non-dogmatic approach to problem resolution that takes advantage of the varied institutional mechanisms afforded by society (e.g., markets, governments, social enterprise, and community-based efforts). Thus, social entrepreneurship is not specifically about creating market mechanisms or securing government subsidies or creating a social enterprise, it is about crafting effective and sustainable solutions using whatever combination of institutional means is deemed effective. Interestingly, this suggests that the greatest success for a social entrepreneur would be to tackle a problem with positive externalities in such a way that the externality is internalized for the benefit of society and the work of the social entrepreneur is no longer necessary. Note that this same outcome of redundancy would represent a failure for commercial entrepreneurs seeking to maximize value capture through sustainable advantage for their venture. While true commercial entrepreneurs who care for value capture try to become indispensable, true social entrepreneurs who care for value creation try to make themselves dispensable. Naturally, social entrepreneurs often get emotionally attached to their organization and may focus on sustaining the organization more than solving the problem for society. Yet, true social entrepreneurs should invite competition instead of resisting it, since replication of the innovative solutions will increase the value created to society.

**Proposition 3** Social entrepreneurs are more likely to seek sustainable solutions than to seek sustainable advantages.

An important implication of this proposition for the field of social entrepreneurship concerns the focal unit of analysis. The theory of the firm suggests that the organization is the central unit of analysis because it is the locus of capture of rents through residual control rights over resources (Grossman and Hart 1986). If we take seriously the argument that the motivation of social entrepreneurs is value creation not capture, then an implication is that the organization may not be the focal unit of analysis for social entrepreneurship. Sustainable advantages are defined at the level of the firm, which is the unit of accrual of appropriated value. In contrast, sustainable solutions are defined at the level of the system, which is the unit of accrual of created value. Thus, a prediction from my theory is that the central unit of analysis for social entrepreneurship research may be the solution and its underlying business model, not the organization. Business models, defined as the interconnected set of activities that create value by addressing a particular need, is a relatively recent area of enquiry in strategy and organization theory (Zott and Amit 2007). There is much to be gained by understanding what types of business models and strategies can be developed when the main driver of action is value creation not value capture. Shifting the focus away from the organization as unit of analysis also brings social entrepreneurship closer to areas that study organizational processes that are not self-contained within traditional organizations. Thus, research on innovative business models, such as open-source development (O'Mahony 2007), and innovative organizational forms, such as community-based organizations (O'Mahony and Bechky 2008; Peredo and Chrisman 2006), are interesting avenues for development of the social entrepreneurship field.

## Empowerment not Control

Mainstream businesses and commercial entrepreneurs focus on value capture. Although value needs to be created in order to be captured, commercial organizations seek to ensure they *control* enough of the industry value chain to appropriate a substantial part of the value they create. The five forces strategy framework is an illustration of that approach (Porter 1980). The organization that better controls key environmental forces can appropriate more value to the extent that the other stakeholders are dependent on the organization, and the organization is not dependent on other stakeholders. There is a whole stream of work in strategy and organization theory that focuses on issues of organizational power and control. Theories such transaction costs economics and resource dependence have the notion of control at their core. The organizations that control critical transactions (Williamson 1991) and resources (Pfeffer and Salancik 1978) can increase survival chances and capture more value.

In contrast, social entrepreneurs are focused on value creation, and their key concern is the effectiveness of the overall value system of activities and partners, not their organization. This means that they do not need to use a logic of control to ensure value capture. Instead, evidence suggests that they use a logic of *empowerment*, which is the opposite of control.

Empowerment, according to the World Bank (2009), is the "process of increasing the assets and capabilities of individuals or groups to make purposive choices and to transform those choices into desired actions and outcomes." It is symptomatic of the pervasive focus of organization theory on issues of power and control that there is so little management research on empowerment beyond the idea of employee empowerment. In fact, employee empowerment can be seen, cynically, as just another mechanism for value capture since firms seek to control the rents generated by the empowered employees' output. Indeed, empowerment schemes are often resisted by employees (Maynard et al. 2007).

In contrast, a central element of the social entrepreneurship approach is the empowerment of actors outside the organizational boundaries (which are often diffuse), be they beneficiaries, users, or partners. Given that social entrepreneurs face severe resource constraints (due to low value capture potential and the lack of societal awareness to the problem that they are addressing) and that they are targeting potentially large-scale problems for which they seek sustainable solutions, the best way to achieve their desired outcomes is to empower beneficiaries and potential stakeholders to become an integral part of the solution. Social entrepreneurs thus typically put in place mechanisms and systems that reduce their stakeholders' dependencies on the organization and increase these stakeholders' ability to contribute to the solution and to their own welfare.

A key element for an empowerment approach is the belief that the beneficiaries or users of the system, no matter who they are, are likely to be endowed with resources and skills that are sub-utilized. In the book "The Mystery of Capital," Hernando de Soto documented the vast amounts of wealth that low-income populations hold in savings and in the value of the homes they live in. Yet, these populations cannot use these assets as collateral for investing in their own economic progress due to a lack of institutions and functioning property rights systems (de Soto 2000). Likewise, de Soto recognizes that low-income populations everywhere in the world are as entrepreneurial and resourceful, if not more, as those in the more developed countries. The proposed solution is to establish a framework that enables people to deploy these resources and skills. While de Soto advocates macro-institutional reforms in property rights and the rule of law to unlock this hidden capital, social entrepreneurs tend to develop micro-institutional solutions. An example is the Gram Vikas perpetual village fund that transforms the savings of rural villagers into an endowment that ensures the operation of the water and sanitation system in perpetuity (Chowdhury and Santos 2011). Gram Vikas estimates that the villager funds are five times larger than the capital that Gram Vikas needs to mobilize on it own (Elkington and Hartigan 2008), which creates a sixfold leverage on its efforts. This is just an illustration of the attractiveness of an empowerment approach.

**Proposition 4** Social entrepreneurs are more likely to develop a solution built on the logic of empowerment than on the logic of control.

A striking example of a solution built on the logic of empowerment is the Barefoot College established in India in 1971 by the social entrepreneur Bunker Roy (Elkington and Hartigan 2008). The founder believes that we have "a gross underestimation of people's infinite capacity to identify and solve their own problems with their own creativity and skills, and to depend on each other in tackling problems. What I learned is that empowerment is about developing that capacity to solve problems, to make choices, and to have the confidence to act on them" (Roy and Hartigan 2009). Over 35 years, Barefoot College has used a grass-roots and practical approach to train and develop almost illiterate people into experts in critical areas such as irrigation and water, solar-powered systems, medicine, architecture, mechanics, and accounting. These graduates then find work in rural villages or stay at the college campus (which was built by its own graduates and is managed collectively by the rural poor). The College work reaches close to 600 villages in India and its graduates have already achieved impressive technical successes. In addition, 20 colleges were already created across 13 Indian states using the Barefoot college template.

There are also some recent examples of empowerment in management practice, in particular with the rise of open-source business models, of which the open-source software movement is a prime example. Corporations that are focused on value capture have been struggling to understand how best to incorporate these principles into their own organizations in a consistent way (O'Mahony and Bechky 2008). One of the most publicly discussed examples of empowerment in the commercial sector was the empowerment of the community of users at eBay. This community had a strong voice on how the platform was managed and took over important functions in the system (such as rating fellow users). Interestingly, this empowerment approach may have been initially driven by the ambivalence of the founders between social and commercial entrepreneurship, as described earlier in the paper. The innovative design of eBay's business model was a source of strength for the company and allowed it to get traction and grow at a time when powerful competitors in online auctions were already well established, such as the publicly listed firm Onsale. Yet, when eBay received venture capital funds and planned an initial public offering of its shares, it became focused on value capture. This led to a permanent tension between the power of the user community and the profitability of the organization. Different value capture strategies such as price increases and additional services offered only to the most profitable users met with fierce resistance from the community. Such tension does not exist in business models focused on value creation, such as Wikipedia, in which the users are empowered to contribute with content and to improve the quality of the existing content, developing what is effectively a public good produced by a global community: a repository of the world's knowledge freely accessible to all.

Overall, exploring how social entrepreneurs use empowerment approaches and embed them in their business models, may not only contribute to the development of social entrepreneurship but also provide compelling ideas about how mainstream organizations, and entrepreneurs can use the concept of empowerment to innovate in their business.

## Discussion

I argue in this article that social entrepreneurs provide a distributed mechanism for society to identify neglected problems with positive externalities, develop innovative solutions to address them and, often, change institutional arrangements so that the externality becomes visible and is internalized by other societal actors. I also clarified how social entrepreneurship is different from commercial entrepreneurship, charity, and government provision. Table 1 summarizes the role of different institutional actors.

An important consideration is the distinction between social entrepreneurship and social activism, two activities that are often confused in practice. Part of the confusion is that negative externalities can be seen as the flip side of positive externalities. For example, trying to prevent companies from polluting (a social activist behavior that generates value by canceling negative externalities) may look similar to building a system for companies to recycle (a social entrepreneurial behavior that brings positive externalities). Indeed, sometimes individuals or organizations take the role of both social entrepreneurs and social activists. For example, Anita Roddick not only built *The Body Shop* with a social entrepreneurial orientation, transforming the cosmetics value chain in a way that addressed environmental and health externalities, but also heavily committed the company as a social activist by developing awareness and pressure campaigns in areas such as human rights and banning animal tests (Pless 2007). Yet, although often deployed in parallel, the underlying activities and requirements of these two domains are different. Social activism is inherently a political activity. It requires exerting pressure on governments and corporations using political mechanisms (demonstrations, strikes, civil disobedience, data gathering to build arguments, and garnering public support). Their goal is not to develop sustainable solutions to problems but, rather, to develop actions that force or influence other societal actors to change their behavior in ways that reduce perceived negative externalities. Although this is an important role in the functioning of the economic system, I argue that social activism does not constitute social entrepreneurship, despite being often included in the broad tent that the field of social entrepreneurship has turned into (Sen 2007). Social entrepreneurship is not about exerting pressure or raising awareness but rather about developing and validating a sustainable solution to problems that often have a local expression but global impact. It is about exploiting opportunities for value creation that were neglected by other institutional actors. It is also about facilitating the dissemination of the solution so that others are compelled to adopt it as well. This process involves innovation and leading by example as opposed to pressuring. In summary, both social activism and social entrepreneurship have important functions in the economic system but they constitute different processes with different institutional goals, although they sometimes co-exist in the same individuals and their organizations (Pless 2007).

### Searching for and Measuring Positive Externalities

The development of the field of social entrepreneurship may require further work on identifying and measuring which externalities are likely to get neglected by both markets and governments. In particular, industry-based analysis should be developed on the impact of solving certain classes of problems whose solutions may have positive spillovers. What is the value for society of curing blindness in one individual? What is the value of eradicating a contagious disease? What is the value of integrating formerly disenfranchised members of society?

**Table 1** Institutional actors in modern capitalist economies

| Characteristics | Governments | Charity | Commercial entrepreneurship | Social activism | Social entrepreneurship |
|---|---|---|---|---|---|
| Distinct role in economic system | Centralized mechanism through which the infrastructure of the economic system is created and enforced (and public goods provisioned) | Distributed mechanism through which economic outcomes are made more equitable despite uneven resource endowments | Distributed mechanism through which through which society's resources and skills are allocated to the most valued activities | Distributed mechanism through which behaviors that bring negative externalities are selected out | Distributed mechanism through which neglected positive externalities are internalized in the economic system |
| Dominant institutional goal | Defend Public interest | Support disadvantaged populations | Achieve competitive advantage | Change social system | Deliver sustainable solution |
| Dominant logic of action | Regulation | Goodwill | Control | Political action | Empowerment |

What is the value of creating a repository of knowledge easily accessible to all? Addressing these questions and developing new metrics would allow comparing the impact of different social entrepreneurship activities. This, in turn, would enable the allocation of societal resources in more efficient ways to areas of greater impact per unit of resource used.

A case in point is that venture philanthropy organizations and social venture capital firms are springing up in large numbers[2] to invest societal resources in the social entrepreneurship organizations capable of achieving the greatest impact (Scarlata and Alemany 2011). The development of value creation benchmarks would be useful for the allocation of resources since the traditional metric for venture capital investments (the potential for profitability) is not valid for social entrepreneurship. Such benchmarks would also help social enterprises allocate resources to different activities or segments of beneficiaries. If we take seriously the notion that there is no dichotomy between social and economic value, then we need reliable ways of measuring the value to society created by different economic activities.

Although this may seem a challenging task, it is not much different from the need to build detailed actuarial tables to assess risks and costs in the insurance industry, or detailed depreciation tables for assets by the accounting profession, or detailed methodologies for cost/benefit analysis for public investment projects. We have more than a century of investments in metrics to support the insurance, accounting and public policy fields. We have only recently started to develop an equivalent knowledge infrastructure for social entrepreneurship and social investing. This will be a fundamental area for the field's progress.

### Self-Interest and Other-Regarding

It is important to note that the theory of social entrepreneurship proposed in this article is consistent with mainstream economic arguments except in one aspect—the assumption of self-interest of economic actors as a basis for economic action, a concept first introduced by Adam Smith in his seminal work on "The Wealth of Nations." Smith argued, among other fundamental economic insights, that the pursuit of self-interest by individuals in free-market competition would lead society to more efficient economic outcomes than those provided by the heavy hand of public interest or the benevolence of individuals (Smith 2003). Since then, from agency theory to transaction costs economics, to the economic theories of the firm, the central assumption about human behavior has been that economic action is driven by self-interest. Although work on economic sociology and business ethics (Jones et al. 2007) has argued persuasively that behavior is influenced by the social and relational context of individuals, economic theory has so far largely failed to integrate other drivers of behavior in mainstream economic models (Rocha and Ghoshal 2006).

Yet, even Adam Smith, the father of "the invisible hand," acknowledged that human behavior is often driven by a sense of sympathy toward others. In his other seminal book, "The Theory of Moral Sentiments" Smith described the mechanisms through which a sense of attachment and desire to help others becomes an important element for individual action and personal fulfillment (Smith 1976). Human beings have an ability to imagine themselves in other's situations and thus empathize with their plight as well as take pleasure from their success. This means that the utility of individuals is connected to the well-being of others, even if they have never met them. This phenomenon of *other-regarding* as opposed to self-interest has a long tradition in ethics research (Jones et al. 2007).

Despite Smith's observations about the multifaceted nature of human behavior, the economists that followed his ideas have failed to explore the impact of other-regarding as a driver of economic behavior. It is as if individuals operate in two distinct spheres: a personal sphere of family and social ties driven by other-regarding, and an economic sphere of resources and production driven by self-interest. Yet, the growing importance of economic actors that behave as if motivated by a regard for others (creating social enterprises, volunteering in charities, and pursuing social missions in their organizations) seems to negate the validity of this partitioning approach to human behavior. Economic theory needs to acknowledge the role that other-regarding behavior plays in economic activities, which may be as important for economic outcomes as the role that self-interest plays.[3]

## Conclusion: Social Entrepreneurship as the Enabler of the Second Invisible Hand

The goal of this article was to place social entrepreneurship in the context of the dialog about economic organization and the functioning of modern economies. The phenomenon of social entrepreneurship challenges our assumptions

[2] For example, the European Venture Philanthropy Association counts more than 100 Funds as members.

[3] Indeed, there is increasing empirical evidence that a narrow focus on self-interest does not capture well the motivations and behavior of economic actors. For example, research on marketing as shown that people are happier when they spend money on others than on themselves (Dunn et al. 2008).

about human behavior and economic action. It also challenges our beliefs about the role of entrepreneurship in society. Social entrepreneurship is an innovation process in the economy that can happen in different institutional contexts, is based on value creation, and operates by its own rules and logic. It is an approach that seems well suited to address some of the most pressing problems in modern society and improve capitalism.

Going back to Adam Smith's ideas of a benevolent invisible hand that turns self-interested individual behaviors toward socially optimal outcomes, the process of social entrepreneurship enables the second invisible hand of the economic system, this one based on other-regarding rather than self-interest. By pursuing their regard for others and addressing opportunities for value creation in a distributed way, social entrepreneurs drive the economy closer to an efficient outcome by systematically identifying neglected problems with positive externalities and developing mechanisms to incorporate these externalities into the economic system. In this regard, social entrepreneurs enable the capitalist system to better pursue its original intent of shared prosperity (VanSandt et al. 2009). Moreover, the distributed nature of their action allows social entrepreneurs to be more effective in this role than a benevolent central actor such as the government. Government leaders, even if motivated by public interest, may find impossible to identify socially optimal outcomes in a myriad of sometimes incompatible individual (and group) preferences (the paradox of social choice in welfare economics). Thus, much in the same way as a benevolent central actor is inefficient at allocating resources to the most productive opportunities and needs to harness the invisible hand of distributed *self-interested* action to generate efficient outcomes, central actors also need to harness the invisible hand of distributed *other-regarding* action to generate even more efficient outcomes.

In the words of Muhammad Yunus, referring to the current inability of modern economies to solve societal problems, "things are going wrong not because of *market failures*. The problem is much deeper than that. Mainstream free-market theory suffers from a *conceptualization failure*, a failure to capture the essence of what it is to be human" (Yunus 2007). Bringing social entrepreneurship into the fold of economic and strategy theory may allow us to better capture in our theories "the essence of what is to be human." I hope to have provided with this article a conceptual framework that can help explain the phenomenon of social entrepreneurship and enable further scholarly research and more effective practice and public policy.

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