EXPANDED ABSTRACT

Innovation applied to financing of enterprises of social economy. A case of impact investment

The economic and financial crisis of 2008 caused a significant mistrust to the capitalist system. After the crisis, different initiatives of capital investors emerged to direct their investments to organizations and projects that would have a social and / or environmental impact. Among management scholars and practitioners such investments are known as impact investments.

Impact investments represent a new financing formula for projects that have a social and / or environmental impact, as well as an economic return. Investors who provide financial resources to these types of projects tend to prioritize social or environmental impact, to economic profitability. That is, they are willing to obtain a lower return in comparison with a conventional investment, as long as they can compensate for it with the achievement of a measurable social and / or environmental impact.

The impact investment market, like any other market, is a combination of capital demand to finance impact generating projects, impact capital supply, and intermediaries that help connect supply and demand. Currently, the impact investment market has developed significantly in countries such as the United States and Canada, as well as some European countries, such as the United Kingdom, The Netherlands and Denmark. These countries have been pioneers in the use of this financing formula for social projects.

Given the growing importance of the impact investment market among practitioners, as well as an increasing interest towards this phenomenon among scholars, this study is aimed to research the concept of impact investment, and puts forward a twofold objective. First, the study aims to perform a descriptive analysis of the concept and characteristics of impact investments, as well as the main existing research lines. Second, the authors present a case of the application of impact investments to finance the growth of a social enterprise.

Specifically, the authors have used the descriptive single case study method. In order to select the exemplary case for the single case study, the purposeful sampling technique is applied, which is considered especially suitable for the objectives of construction and extension of theory. Specifically, the authors have looked for a social enterprise that, on the one hand, has a clear social impact in the core of its main activity, and on the other hand, aims to economic sustainability instead of philanthropy. To choose the unique case the database of 519 social enterprises prepared by the Generalitat de Catalunya has been scrutinized. More than 50% of the social enterprises in this database are work inclusion companies, so this sector has been chosen as the most representative and important for the social and solidarity economy of Catalonia.

In the preliminary analysis the study has excluded non-profit organizations whose main reason for including people with disabilities was purely philanthropic and not aligned with the main business. As a result, only one was chosen because of its relevant impact on the local and international community – a design studio La Casa de Carlota (LCDC).

During its five years of existence, this social enterprise has grown from a newborn start-up, to a company with a broad customer base and a subsidiary in Latin America. LCDC has reached the break-even point in 2017, and is now in the phase of expansion. During these years, the funding strategy has been changing according to the needs of the enterprise.

Although there are certain similarities with a conventional start-up, the financing strategy has always been marked by its purpose of creating social impact. In particular, the enterprise avoided conventional investors that would look for economic profit maximization, and would turn to investors that prioritize its social impact. As the results the enterprise turned to impact investors, who did not seek short-term financial profitability, but rather prioritized creation of social impact and long-term economic sustainability. In the case of LCDC, impact investors were two non-profit foundations.

The study shows that the funding process was not an easy task for the enterprise. First, there were difficulties to measure the social impact generated. According to its founders, the impact generated by the inclusion in the work team of people with intellectual disabilities is evident, but they do not have tools to quantify this impact. In this sense, they consider that this lack of resources for measuring social impact can be an important obstacle for social enterprises to receive financing from impact investors.

Second, investment strategies of impact investors, like foundations, are characterized by being conservative and cautious. This fact had a negative impact on LCDC, because these foundations do not usually make large capital injections at once, but instead distribute them over a period of time. This fact affected LCDC’s growth strategy.

There were, however, positive features in choosing impact investors as well. An interesting singularity of the impact investment was the relationship between the investor and the social enterprise. In this sense, LCDC treated its investors not only as financing providers, but as partners, linking investors in the main activity of the company, taking advantage of their experience, and treating them as team members.

Finally, the intermediary platform between LCDC and the investment foundations was of great importance so that the company could be financed through impact investors. In the case of LCDC, it was the Ship2B platform, which not only helped to connect the two agents, but also helped in the development of the action plan, the estimation of the value of the company, and the contribution of technical knowledge to the project.

The study has some limitations. First, it only presents a single case study, which limits the generalizability of its results. The choice of this methodology was conditioned by the objectives of the study, which is to analyze a sample case of a funding strategy of a social enterprise through impact investors. However, more quantitative research should be done to contrast the results of the qualitative study. Second, the specific case of a social enterprise of work inclusion has been chosen. A cross-case comparative analysis that would include social enterprises from various industries is needed to shed more light on the nature of impact investment industry.

The study has important implications for both scholars and practitioners, because it helps to understand the nature of impact investments and sheds light on this new ecosystem. Social enterprises and impact investors occupy an important place in the economies of both developed and developing countries, and academic researchers have to pay more attention to this new type of economy.

We contribute to the existing academic research by presenting an analysis of a case of the use of this financing instrument in the growth of a company with social impact, dedicated to design and communication. In 2016, the company closed a funding round with several impact investors. The analysis of this experience has shown that the alignment of objectives around the generation of social impact, was a key factor for the understanding between the two. However, the lack of tools to measure the social impact and caution of investors were factors that conditioned the growth of the company.

KEYWORDS: Impact investment, social and environmental impact, social enterprise, social finance, third sector.