UNIT 3
Social Ventures

A **social venture** (also called a social enterprise) is undertaking by a firm or organization established by a social entrepreneur that seeks to provide systemic solutions to achieve a sustainable, social objective.

Social ventures may be structured in many forms, including

- sole proprietorships,
- For-profit corporations,
- nonprofit organizations,
- non-governmental organizations,
- youth groups,
- community organizations, and more

Typically, government organizations are not considered to be social ventures.

The distinguishing characteristic of the social venture versus the commercial venture is

- the primacy of their objective to solve social problems and provide social benefits.
- The social venture may generate profits, but that is not its focus. Rather profits are a possible means to achieve sustainability in providing a social benefit.
- The problems addressed by social ventures cover the range of social issues, including poverty, inequality, education, the environment, and economic development.

- The context in which social ventures operate is very complex as they are trying to bring about solutions where markets or governments may have failed or actually impede solutions.
- Further, these ventures are trying to provide solutions where money is usually in short supply—often these ventures have little assurance that their services can be paid for by those they seek to serve.

Addressing persistent social problems

5 Ways an Entrepreneurial Mindset Helps Solve Social Problems

Entrepreneurs possess many valuable skills that apply to nonprofits. So when adopting an entrepreneurial mindset at your nonprofit, start by considering how this approach can translate into meaningful solutions to today's social challenges.

1. Entrepreneurial Thinking Combines Creativity With Market Intelligence

Entrepreneurial thinking naturally embodies creativity—a boundless imagination of what's possible. But the most successful entrepreneurial endeavors balance creative solutions with comprehensive market intelligence.

Successful entrepreneurs start with a solid understanding of the problem. They can explain why it's a pressing need, then back that assertion up with relevant data. In addition to identifying an existing social problem, they look at how it's been addressed historically. That's where their creativity comes in.

So rather than tinkering away at current solutions in hopes of incrementally improving, entrepreneurs decide those approaches are not good enough. They seek new ideas to address social problems with exponential improvement.

For example, passionate individuals start nonprofits when they've identified a specific problem and feel called to solve it. Over time, they may get comfortable with their current programming or approach. But entrepreneurial thinking reminds nonprofit leaders to ask "what if?" and brainstorm new, creative solutions that could take their organization to the next level.

2. Entrepreneurial Thinking Centers Around Lived Experiences

In traditional business models, customers are the recipients of a product or service. On the other hand, entrepreneurial business plans view customers as active participants in the product or service. The latter seeks customer feedback, asks for business ideas, and creates customer-focused messaging. And the result is the best possible product or service for those using it.

This same entrepreneurial mindset helps drive crucial change in solving social problems, as nonprofits can ask beneficiaries what they most want and need. This feedback informs optimizations to program designs or sparks innovations for new approaches to solving the problem.

3. Entrepreneurial Thinking Considers Measurable Impact and Sustainability

Entrepreneurship aims to make lasting positive change—it's not enough to solve an issue once if the root cause of that problem persists. As part of entrepreneurial project management, creative thinkers detail their plans and describe how they'll measure their success. Ensuring a concept's sustainability in its initial design is critical to a successful outcome.

This type of entrepreneurial thinking can help nonprofits anticipate potential roadblocks and challenges and establish a mitigation strategy proactively. It also allows nonprofits to move toward solving the issue's deeper causes instead of just fixing the surface cracks.

Additionally, donors may find this element of entrepreneurial thinking attractive when considering which organizations to support. It shows accountability for using donor funds effectively and identifying when it's time to make changes.

4. Entrepreneurial Thinking Embraces Risk and Failure

Funding protocols, public perception, and the significance of the problems nonprofits address have contributed to a risk-averse approach in the social sector. But unfortunately, ideas that drive dramatic change are inherently risky propositions and present the potential to fail. Entrepreneurial thinking acknowledges that uncertainty and accepts it as a necessary driver of progress.

Organizations run by entrepreneurial-minded leaders know that new ideas put them at risk for huge potential losses. Their missions are big and bold, but they know the rewards far outweigh the risks. And if failures arise, entrepreneurial thinking helps leaders quickly reframe those as learning opportunities to make adjustments and try again.

5. Entrepreneurial Thinking Adopts a Bold Vision for the Future

Big problems require big solutions, and entrepreneurs often live by a “go big or go home” mentality. Because of that, incremental change is insufficient for entrepreneurs—they demand monumental change toward a gutsy endgame.

Entrepreneurial thinking helps solve social problems by not shying away from the biggest, most challenging topics. Instead, the mindset focuses on what *is* possible. In other words, entrepreneurial thinking has the potential to inspire your nonprofit’s vision statement for what the world will look like as a result of your impact.

Financing Social Ventures

DIFFERENT TYPES OF SOCIAL VENTURE FUNDING

Social enterprise accelerator programs are specifically designed to help social entrepreneurs create and grow sustainable for-purpose businesses. Whether you're in ideation phase or already in operation, a pit stop at a social enterprise accelerator is a great way to fast track your progress.

As the sphere of social entrepreneurship has expanded in the past few years, so too has the number of accelerators (and incubators). In general, these programs offer a combination of access to experienced entrepreneurs and mentors, business model refinement, start-up capital, and the opportunity to pitch to potential investors.

Social impact incubators provide a supportive environment for social entrepreneurs to develop their ideas and turn them into viable social enterprises. They provide resources such as business planning advice, networking opportunities, and access to funding. Social entrepreneurs often face significant challenges in launching their businesses, including securing funding, building networks, and navigating complex regulations. Social impact incubators help to overcome these challenges and support the growth of social entrepreneurship.

Social venture capital (SVC) is a type of ***private equity investment*** that is made with the intention of **achieving a positive social or environmental** impact alongside a financial return.

SVC is a relatively new concept, but one that is gaining traction as more investors look to put their money into businesses that are having a positive impact on society or the environment.

There are a number of different ***social impact investing*** strategies that venture capitalists can pursue, but all involve making investments in companies or projects that are expected to generate both financial returns and social or environmental benefits.

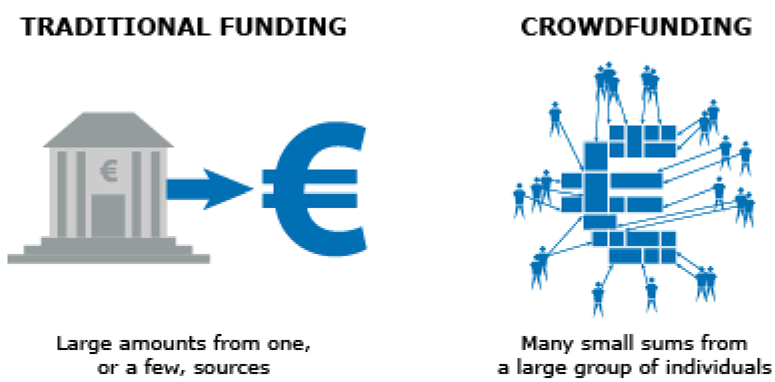
One of the most common types of ***social venture capital*** investment is in early-stage companies that are working on innovative solutions to social or environmental problems. These businesses often have difficulty accessing traditional sources of capital, so SVC can be an important source of funding.

An angel investor provides initial seed money for startup businesses, usually in exchange for ownership equity in the company.

The angel investor may be involved in a series of projects on a purely professional basis or may be found among an entrepreneur's family and friends. The investor's involvement may be a one-time infusion of seed money or an ongoing injection of cash to get a product to market.

Angel investors aren't usually in the loan business. They're putting money into an idea they like, with the expectation of a reward only if and when the business takes off.

Crowdfunding is a way of raising money to finance projects and businesses. It enables fundraisers to collect money from a large number of people via online platforms.



Crowdfunding is most often used by startup companies or growing businesses as a way of accessing alternative funds. It is an innovative way of sourcing funding for new projects, businesses or ideas.

It can also be a way of cultivating a community around your offering. By using the power of the online community, you can also gain useful market insights and access to new customers.

This guide is aimed at entrepreneurs, business people and companies, especially small and medium enterprises. If you are thinking about ways of financing a new business or idea, or have heard about crowdfunding and want to learn more, you may find this guide useful.

Bootstrapping in the startup context refers to the process of launching and growing a business without external help or capital. It involves starting from the ground up, using personal savings and/or existing resources instead of relying on investors or loans. Bootstrapping often involves creative problem solving and finding creative ways to get things done without spending a lot of money.

Startup business grants provide free funding to help small businesses grow without debt. However, competition for small-business grants is fierce, and many awards require time in business — often at least six months.
Some grants are open to newer businesses or true startups. And even if you don't qualify now, it can pay to know where to look for future funding. Here are the best grants for small-business startups, plus alternative sources of startup funding to consider.

4 startup valuation methods used by VCs and angels

As an entrepreneur seeking to raise funds, you probably know that startup valuation often relies on guesswork and estimation, so there's no single, universally accepted analytical methodology for investors.

Instead, venture capitalists and angel investors draw upon several venture capital valuation methods to understand the value of a startup.

The use of startup valuation methods is dependent upon the stage of your business and the corresponding data points available in your startup's market and/or industry your startup operates in (earnings/revenue/acquisition multiples etc.).

In this article, we'll take you through the 4 most commonly used early-stage and pre-revenue angel and venture capital valuation methods to help you understand how potential investors may assess your business.

In the meantime, if you'd like an idea of what yours might be, use our startup valuation calculator.

1. Venture Capital Valuation Method
2. Scorecard Valuation Methodology
3. Dave Berkus Valuation Method
4. The Risk-Factor Summation Method

1. Venture Capital Valuation Method

The VC Valuation Method was first introduced in 1987 by Harvard Business School Professor Bill Sahlman. It can be used by venture capitalists and angel investors to work out pre-money valuation by first determining post-money valuation, using industry metrics.

The methodology is simple and stems from the following equations:

Post-money valuation = terminal value / anticipated ROI

Pre-money valuation = terminal value / post-money valuation

2. Scorecard Valuation Methodology

The scorecard startup valuation method compares your company to similar angel-funded startup ventures and adjusts the average valuation of recently funded companies in the industry to establish a pre-money valuation of your startup. Such comparisons can only be made for companies at the same stage of development.

How does the Scorecard Valuation Methodology work?

Step 1 – Determine the average pre-money valuation

A venture capitalist or angel investor will determine the average pre-money valuation of pre-revenue companies in your business sector. Pre-money valuation varies with the economy and the competitive environment for startup ventures within an industry. In most industries, for pre-revenue startups, the pre-money valuation does not differ too significantly from one business sector to another.

Based on Seedrs' data, as of 2019, pre-money valuations vary from £750,000 to £2m for seed stage, pre-revenue companies.

Step 2 – Compare your company to similar deals in your sector

The next step is to compare your company to similar deals done in your sector, considering the following:

Strength of the founder and management team: your experience, skillset, and flexibility as the founder, and the completeness of your management team.
Size of the opportunity: market size for your company's product or service, the timeline for increase (or generation) of revenues, and the strength of competition.
Your product or service: product/market definition and fit, the path to acceptance, and barriers to entry.
The quality of your business plan: the sales channel, the stage of business, the size of the investment round, and the need for financing.

Here is a section of a typical valuation worksheet that has been developed to assess the relative strength of target companies:

Size of Opportunity

1. Size of the specific market for the company's product or service
- > £500m (+2)
- > £100m (+1)
- > £50m (-1)
- < £50m (-2)

2. Potential for revenues in five years?
- > £100m (+2)
- > £50m (+1)
- < £25m (-1)

3. Strength of competition in this marketplace
- Weak (+1)
- Modest (or none) (-1)
- Strong (-1)

Step 3 – Score your startup and calculate its value

You will see that for each comparison factor, like the one shown above, there are a set of multiple-choice questions to answer about your business. The answers give your startup a score in the range of -3 (worst) to +3 (best).

An angel investor or VC would multiply this score against the comparison factor range (see below) to give each section a weighting, then sum up the total factors and multiply this against the average pre-money valuation for your industry to arrive at your startup's estimated valuation.

3. Dave Berkus Valuation Method

Dave Berkus is a widely respected lecturer who has invested in more than 80 startup ventures. Dave's model first appeared in a book published by Harvard's Howard Stevenson in the mid-1990s and has been used by angel investors ever since.

The most recent version of the Dave Berkus Valuation Method updated in 2009, would start with a pre-money valuation of zero, and then assess the quality of your company in light of the following characteristics:

Characteristics	**Add to Pre-Money Valuation**
Quality management team	Zero to £0.4 million
Sound Idea	Zero to £0.4 million

Working prototype	Zero to £0.4 million
Quality board of directors	Zero to £0.4 million
Product rollout or sales	Zero to £0.4 million

For example, if your early-stage business has a good quality management team, a working prototype and sales, your valuation will be estimated at £1.2m following the Dave Berkus method.

Note that the numbers are the maximum for each class so a valuation can be £800,000 (or less) as easily as £2m. Furthermore, Dave reminds us that his method “was created specifically for the earliest stage investments as a way to find a starting point without relying upon the founder’s financial forecasts”.

4. The Risk-Factor Summation Method

The Risk-Factor Summation Method considers a much broader set of factors in determining the pre-money valuation of pre-revenue companies. The Ohio Tech Angels who developed this method, describe it as follows…

“Reflecting the premise that the higher the number of risk factors, then the higher the overall risk, this method forces investors to think about the various types of risks which a particular venture must manage in order to achieve a lucrative exit. Of course, the largest is always ‘management risk’ which demands the most consideration and investors feel is the most overarching risk in any venture. While this method certainly considers the level of management risk it also prompts the user to assess other risk types.”

The most important risks that need to be assessed include:

Management risk
Stage of business
Legislation/political risk
Manufacturing risk
Sales and marketing risk
Funding/capital raising risk
Competition risk
Technology risk
Litigation risk
International risk
Reputation risk
Potential lucrative exit

Each of the above risks is then assessed as follows:

+2	very positive for growing the company and executing a lucrative exit

+1	positive
0	neutral
-1	negative for growing the company and executing a lucrative exit
-2	very negative

INHOUSE CORPORATE FUNDING MECHANISM

What Is In-House?

In-house refers to an activity or operation that is performed within a company, instead of relying on outsourcing. The firm uses its own employees and time to perform a business activity, such as financing or brokering.

This is the opposite of outsourcing, which involves hiring outside assistance, often through another business, to perform those activities.

Understanding In-House

The determination as to whether to keep activities in-house or to outsource often involves analyzing the various costs and associated risks. How these costs are calculated may vary depending on the size and nature of the core business.

A firm may decide to keep certain activities in-house, such as accounting, payroll, marketing, or technical support. While it can be cheaper to outsource those divisions, there are also circumstances where it pays to invest in in-house professionals.

Additionally, keeping these activities in-house may allow the business to exert higher levels of control by keeping the services and personnel under direct control. There may also be fewer security risks depending on the kinds of data that would have to be supplied to an outside party should the activity be outsourced.

At times, internal employees may have a better understanding of how the business functions overall, providing them with insights into how certain activities should be handled, allowing them to function with the business's core vision at the forefront of the decision-making process.

In-House Services

When dealing with customers, a firm may try to keep the entire transaction in-house. For example, in-house financing is a common practice in certain industries. This form of financing works by using the firm's resources to extend the customer's credit, with the firm potentially benefiting from any associated interest payments in exchange for assuming the risk associated with default.

For a brokerage, the firm may try to match a client's order with another customer, creating an in-house transaction. This allows the firm to benefit from both the buy- and sell-side commissions and potentially lowering other administrative costs.

In-house financing is a type of seller financing in which a firm extends customers a loan, allowing them to purchase its goods or services. In-house financing eliminates the firm's reliance on the financial sector for providing the customer with funds to complete a transaction.

Advantages and Disadvantages of In-House Operations

In-house business operations can offer an additional revenue stream, by offering services that the company's clients would otherwise find elsewhere. Auto companies frequently offer in-house financing at higher rates than those available from banks or credit unions.

In addition, conducting business operations in-house gives a company greater control over the execution of these operations, since it is the direct employer of the teams conducting those operations.

The main disadvantage of in-house operations is the cost of maintaining an additional team, that may be outside of the company's core business. Many companies outsource their payroll, IT, or other technical work, because the companies are too small to justify hiring full-time staff for these roles.

Pros and Cons of In-House Operations

Pros

- In-house services can provide some retailers with additional revenue streams.
- Companies have more control over in-house teams than they would with a contractor.

Cons

- In-house operations can be more expensive and take resources away from the company's core business.
- Smaller companies might not have enough work to justify hiring full-time in-house staff.

Real-World Example of In-House Financing

Ford Credit is a well-known in-house auto financing group. Ford Credit is the business of giving out auto loans for Ford car buyers at their own dealerships, rather than encouraging Ford customers to seek external financing from a bank or credit union.

In January 2017, Ford Credit partnered with AutoFi to make car buying and financing even easier through technology that allows the buyer to shop online for their car and auto loan. With this new point-of-sale platform, Ford customers can shop online through Ford dealer websites, buy and finance their car. This type of customer experience allows car buyers to spend less time at the dealership while also offering a faster sales process for Ford. Other auto companies such as General Motors also have important in-house financing arms

What is Microfinance?

Microfinance refers to the financial services provided to low-income individuals or groups who are typically excluded from traditional banking. Most microfinance institutions focus on offering credit in the form of small working capital loans, sometimes called microloans or microcredit. However, many also provide insurance and money transfers, and regulated microfinance banks provide savings accounts.

Microfinance aims to improve financial services access for marginalized groups, especially women and the rural poor, to promote self-sufficiency.

Microfinance and Financial Inclusion

Low-income people are neglected by their financial systems because they are considered uneconomical to serve or too difficult to reach. According to the World Bank's Global Findex, 1.7 billion adults globally are financially excluded, living without formal credit or savings.

Microfinance seeks to address the needs of the unbanked by fostering economic justice and financial inclusion for all.

Benefits of Microfinance

Access to essential financial services can empower individuals economically and socially by creating self-reliance and economic sustainability in impoverished communities where salaried jobs are scarce. The benefits of microfinance include:

- Small loans enable entrepreneurs to start or expand micro, small and medium enterprises.
- Savings help families build assets to finance school fees, improve homes (e.g., install power or running water) and achieve goals.
- Insurance products can offset the cost of medical care.
- Money transfers and remittances allow families to easily send and receive money across borders.

Hundreds of millions of low-income people have benefited from microfinance since its inception, with about 140 million borrowers served by the industry worldwide annually.