2 Mapping the Field: Social Business and Relevant Contexts

Since Muhammad Yunus, the founder of the Grameen Bank in Bangladesh, first coined the term "social business" through his Nobel lecture in December 2006, the notion has become a popular buzzword. Universities and business schools across the globe have established so-called Institutes or Labs for Social Business. In Germany, the number of companies and consultancies carrying the term in their name has been booming, while the first South Asian Social Stock Exchange (IIX) is about to emerge in Singapore[4]. Though Yunus is the main reference point for most of these initiatives, definitions remain vague and interpretations differ. Meanwhile, Yunus has created several social business companies in order to prove his theoretical concept (YUNUS 2010a). Combining a macroeconomic claim ("creating a world without poverty") with a micro-level implementation strategy (through non-loss, non-dividend companies), Yunus' social business approach touches upon several cross-disciplinary research areas of interest to political and business economists as well as social scientists. This also holds true for human geographers. Yunus' activities pose fundamental questions about global poverty, corporate social responsibility (CSR), and the future of development aid. How exactly does Yunus envision what he calls a new kind of capitalism? What's the difference between social business companies, non-profit enterprises, or businesses at the base of the pyramid (BOP)?

Though the empirical part of this study has a focus on poverty reduction through social business at a micro-level, this chapter aims to briefly explore the most relevant academic and policy contexts with respect to the research at hand. Taking Yunus' concept and experiments as a starting point, this **mapping exercise** will reveal distinctive characteristics of (Grameen) social business and result in its classification as a new hybrid entity that combines elements of both traditional non-profits and profit-maximizing businesses. The following mapping exercise does not claim to be exclusive or catholic. It rather intends to position social business as a dynamic research field at the intersection of various academic disciplines, while at the same time contributing to a **conceptualization** of the term itself. Subsequently, the research status will be confined to (Grameen) social business.

The chapter is organized into five sections as visualized in Figure 2. Major findings will be summarized at the end of each section.

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4 In parallel, but in a completely different sense, the term social business is becoming popular in web communities where it is used with reference to social media applications in for-profit companies. This understanding is not part of the investigation at hand.

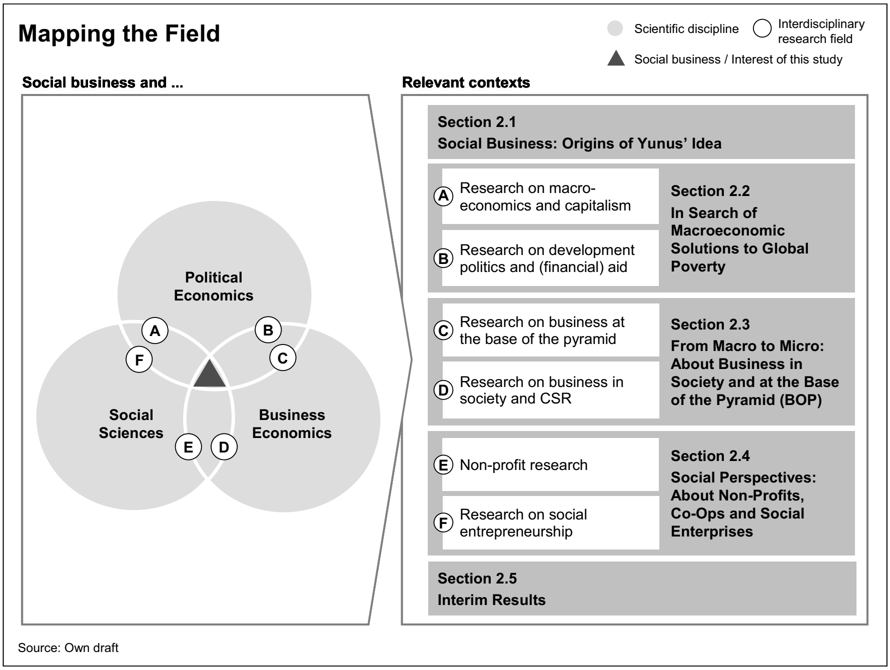

Figure 2: Social Business and Relevant Contexts

2.1 Social Business: Origins of Yunus' Idea

Fair loans to poor people without any financial security appeared to be an impossible idea, but from modest beginnings three decades ago, Yunus and Grameen Bank have contributed to a micro-credit revolution across the globe. Starting with a brief introduction to Grameen Bank and its core principles, this section will outline how Yunus' social business idea has evolved over time. Subsequently, key features of the concept will be explained, followed by a brief excursus on the notion's literal roots.

2.1.1 The Grameen Bank Experiment

Grameen Bank (literally meaning village bank in Bangla) is a community development bank that provides collateral-free loans and banking services to the rural poor. Muhammad Yunus, a former Professor of Economics, founded the bank on a belief that access to capital could transform human lives. The idea was born in 1976 when Yunus, then head of the Rural Economics Program at the University of Chittagong, loaned US$ 27 from his own pocket to 42 people in the Bangladeshi village of Jobra. At that time, Yunus realized that local women who crafted bamboo furniture didn't profit from their labor due to enormous interest rates and unfair conditions when they were lent money to buy bamboo, and that a fair loan could break the vicious cycle of chronic poverty (YUNUS 1999).

> "I was shocked to discover a woman in the village, borrowing less than a dollar from the money-lender, on the condition that he would have the exclusive right to buy all she produces at the price he decides. This to me, was a way of recruiting slave labor" (YUNUS 2006a: 2).

Since existing banks were not interested in making small loans to the poor, claiming high risks of loan defaults, Yunus turned into an informal banker, guaranteeing loans to the poor by taking personal responsibility for their repayment towards the bank. Coming up with simple rules (e.g., having people pay back their loans in small weekly amounts and having bank officers visit the villagers rather than the other way around), made his borrowers paying back their loans on time (YUNUS 2010a, 2007a). Yunus, nevertheless, kept confronting difficulties when trying to expand his program through existing banks. In 1983, the pilot project was, thus, transformed into a formal bank under a special law passed for its creation (GRAMEEN BANK 2010).

The Grameen Bank Approach

Grameen Bank borrowers have to commit to a philosophy built on four principles: discipline, unity, courage, and hard work. To ensure repayment (despite the lack of collateral against their micro-loans) a group-based credit approach is applied, utilizing peer pressure within groups of at least five women (YUNUS 1999). Repayment solely rests on the individual borrower, but the group oversees that everyone behaves in a responsible way and further credit to a group is provided only after previous loans have been recovered. According to Grameen Bank, the whole system is based on trust and functions without written contracts or legal instruments (GRAMEEN BANK 2010). There are four different interest rates for loans from Grameen Bank: 20% for income generating loans (e.g., used to purchase a cow, seeds, or a cell phone so that borrowers can sell milk, raise crops, or offer phone services), 8% for housing loans, 5% for student loans, and interest-free loans for beggars.

All interest is simple interest, calculated on a declining balance method. In contrast, the Government of Bangladesh has fixed interest rates at 11% (flat rate). According to Grameen Bank, this amounts to about 22% in interest, when calculated in the Grameen way[5] (ibid.). To supplement the lending, Grameen Bank requires its members to save small amounts in a number of funds that serve as insurances against contingencies. In Bangladesh, Yunus' bank also incorporates a set of values embodied in sixteen decisions and borrowers vow to follow them (e.g., send all

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5 According to experts in microfinance, this kind of comparison is actually tricky, because it all depends on the average credit period. But as a rule of thumb, flat rates lead to about double annual percentage rates (see www.mftransparency.org).

children to school; keep the family small; look after their own health; use pit-latrines; drink safe water). Though not about banking, these decisions are an integral part of Grameen's business approach, geared to improving families' wellbeing (YUNUS 1999, 2007a).

Achievements

As of October 2010, Grameen Bank reports to have disbursed more than US$ 9.8 billion to over 8.3 million borrowers, 97% of whom are women who, according to Yunus, are more likely than men to devote earnings to their families (YUNUS 2006a; GRAMEEN BANK 2010). According to Grameen Bank's statements, the number of borrowers has more than doubled since 2003, and the village bank serves over 81,000 villages through more than 2,500 branches in rural Bangladesh. Till today Grameen Bank is owned by its borrowers and remains devoted to providing villagers with collateral-free loans. Since their introduction in 1984, housing loans have been used to construct more than 640,000 houses (GRAMEEN BANK 2010). Financially, Grameen Bank is self-reliant and has not taken donor money since 1995. The Bank's audited recovery rate is at 97 percent which is far higher than the industry standard for loans to those who have collateral. According to Yunus, the bank has actually made a profit every year since it came into being, except in 1983, 1991, and 1992. Deposits and its own resources currently amount to 159% of all outstanding loans.

According to an internal survey, 68% of Grameen borrowers have crossed the poverty line, measured by Grameen's own indicators related to its 16 decisions (YUNUS 1999). Grameen also encourages the children of its borrowers to go to school, offering affordable loans for them to pursue higher education. More than 50,000 students are currently pursuing their education in medical or engineering schools and universities with financing from the village bank (YUNUS 2010a). Meanwhile, the idea of collateral-free micro-loans for poor women has become a global phenomenon. Through its Grameen Trust the village bank has supported 141 direct replication projects in 38 countries in Asia Pacific, Africa, and America – including one that brings micro-credits to single mothers in New York City (GRAMEEN AMERICA 2010). Most of these replications follow the methods Grameen Bank has pioneered – including charging the lowest possible interest rates on loans and giving borrowers the opportunity to become owners of the bank (YUNUS 2010a).

In parallel to the explosive growth in non-profit microfinance institutions, the micro-credit business has attracted for-profit companies including Citigroup and Deutsche Bank, resulting in a 9 billion dollar micro-lending industry (PRASSO 2007; GRAMEEN BANK 2010). Some profit-driven organizations charge interest rates in excess of 80% per year, arguing that managing small loans for the poor is more costly than handling conventional loans (SPARREBOOM et al. 2008). With the explosive growth in microfinance institutions lending terms have also become less restrictive and the poor have resorted to borrowing from a variety of sources (GEHLICH-SHILLABEER 2008). But since more than 50 Indian farmers who couldn't make payments on their multiple micro-loans committed suicide in late 2010, the whole microfinance industry has fallen into disrepute (PINZLER 2010; MADER 2010). For Yunus, who claims that interest rates should not go much beyond the sum of the costs of funds and delivery cost, this is a perversion of his (social) business approach, violating the pro-poor spirit on which the micro-credit model had been created (SPARREBOOM et al. 2008). "Replacing the traditional exploitative village moneylender with a new form of exploitation was not what I had in mind when I founded Grameen Bank" (YUNUS 2010a: 14).

Since the first two microfinance institutions have gone public in 2007 (Compartamos in Mexico) and 2010 (SKS Microfinance in India), the question whether or not increasing commercialization is good for microfinance has been highly contested. While Yunus thinks that profit-oriented microfinance will lead to a drift away from his original premise (i.e., helping the poor), advocates of the profit-oriented model argue that cooperative models are not efficient and scalable enough to meet the global demand for financial services. Tapping capital markets could help to scale the business and competition would eventually bring down interest rates to consumer-friendly levels. Though this kind of debate about pricing, investors, profit, and welfare has its root in a fundamental concern called "mission-drift", it actually overlooks some older critics that go beyond the risk of over-indebtedness (GEHLICH-SHILLABEER 2008). Ten years ago, RAHMAN (1999) had already probed the Grameen Bank model, pointing to widespread exclusion of the poorest women, destructive peer pressure, and an ideology that would go far beyond financial service. The anthropologist also pointed to a phenomenon currently described as consumption smoothing (COLLINS et al. 2010). Many credits were used for consumption which could help to manage poverty but not eradicate it. In this context, KARNANI (2007a) has amplified that it was false to believe that the poor were born to be entrepreneurs. The vast majority of micro-credit borrowers had no specialized skills and were thus caught in subsistence activities or rather micro-credit dependency.

Despite these critics, Yunus and Grameen Bank were awarded the Nobel Peace Prize in 2006 for their "efforts to create economic and social development from below" (NOBELPRIZE.ORG 2006). Today, Yunus is regarded as the spearhead of the modern micro-credit industry, although Friedrich Wilhelm Raiffeisen (1818-1888) from Germany has been recognized for being the one who pioneered the idea of cooperative self-help and rural credit unions.

2.1.2 From Micro-Credits to Social Business

For Yunus, founding a bank for the poor and developing a viable business model to serve their financial needs was what he calls a first step in a journey that still continues (YUNUS 2010a). Today, Yunus promotes the broader idea of social business – a sort of inclusive business dedicated to solving social, economic, and / or environmental problems. To fully grasp the roots of Yunus' entrepreneurial approach, it helps to understand his personal background and idea of man. Though Yunus initially got involved with poverty issues as an academic, his personal exposure to human misery in the backdrop of a famine in Bangladesh in 1974 had a strong influence on his later propositions.

> "I found it extremely difficult to teach elegant theories of economics in the classroom while a terrible famine was raging outside. Suddenly I felt the emptiness of economic theories in the face of crushing hunger and poverty. I realized that I had to leave the campus and somehow make myself useful to the distressed people of Jobra, the neighbouring village" (YUNUS 2009b: 1).

In search of effective strategies to activate the poor, Yunus first created Grameen Bank and later several other organizations trying to encourage entrepreneurship and self-reliance among the poor. Over time he became involved in agriculture, livestock and fisheries, renewable energy, information technology, education, health, and employment services. Since the late 1980s, the Grameen family of enterprises has grown into a multifaceted group of nearly 30 for-profit and non-profit ventures, including companies such as Grameen Software Ltd., Grameen Knitwear Ltd., or Grameen Telecom. The latter has a stake in Grameen Phone, the biggest private sector phone company in Bangladesh. Since its start in 1997, the village phone project of Grameen Phone has reportedly brought cell-phone ownership to more than 400,000 rural women. Acting as phone ladies in over 50,000 villages, they provide customers with access to market information and telecommunication services (YUNUS et al. 2010; GRAMEEN PHONE 2010).

> "Whenever I wanted to deal with a social or economic problem, I tried to solve the problem by creating a business around it. Over time I became convinced that it is an excellent way to address social and economic problems, but one that is missing in the framework of economic theory" (YUNUS 2010a: 17).

Yunus basically reasons that poverty is not created by the poor themselves. The economist conceptualizes poverty as an external imposition resulting from **institutional deficiencies**. To make his point, he often refers to traditional banks that refused to provide financial services to the poor until Grameen Bank started to question previous assumptions about their credit-worthiness, demonstrating that lending to the poor was possible in a sustainable way. Based on this experience, Yunus believes that the existing socioeconomic system has been designed in a way that prevents the poor from unleashing their human potential.

> "We built our theoretical framework on assumptions which underestimate human capacity, by designing concepts which are too narrow (such as concepts of business, credit-worthiness, entrepreneurship, employment), or developing institutions, which remain half-done (such as financial institutions where the poor people are left out). Poverty is caused by the failure at the conceptual level, rather than any lack of capability on the part of people" (YUNUS 2006a: 4).

Expanding Economic Theory

Moving from micro-credit to a broader social business concept, Yunus calls for a fundamental change in the architecture of today's capitalist economy which according to him has led to worldwide poverty (YUNUS 2009b, 2010a). The economist argues that a fundamental flaw in present-day economic theory lies in the misinterpretation of human nature. Those engaged in business were portrayed as one-dimensional beings dedicated to only one mission – to maximize profit. "This was done perhaps as a reasonable simplification, but it stripped away the very essentials of human life", insulating them from all political, emotional, social, spiritual, and environmental dimensions of life (YUNUS 2006a: 3).

> "We have remained so impressed by the success of the free market that we never dared to express any doubt about our basic assumption. To make it worse, we worked extra hard to transform ourselves, as closely as possible, into the one-dimensional human beings as conceptualized in the theory to allow smooth functioning of free market mechanisms" (ibid.).

With reference to churches, non-profits, and volunteer organizations, the economist argues that human beings were not controlled by the profit motive but also driven by altruistic motivations not yet reflected in economics: "The essential fact about human beings is that they are **multidimensional** beings" (YUNUS 2009b: 5), and by defining business (and those engaged in business) in a broader way, the character of capitalism could be transformed, thus opening up new avenues for the solution of unsolved problems. Yunus acts on the assumption that human beings and entrepreneurs respectively have two sources of motivation, mutually exclusive but equally compelling: a) maximizing profit and b) doing good to others (YUNUS 2006a). Each type of motivation translating into a separate kind of institution, he calls the first **profit-maximizing business** and the second **social business**. While the first one was for personal or financial gain, the other was dedicated to helping others.

> "A social business is operated as a business enterprise, with products, services, customers, markets, expenses, and revenues – but with the profit maximization principle replaced by the social-benefit principle. Rather than seeking to amass the highest possible level of financial profit to be enjoyed by the investors, the social business seeks to achieve a social objective" (YUNUS 2007a: 23).

What, according to Yunus, makes a social business a business is commercial viability or rather **economic sustainability**. A social business company has to generate enough income to cover its own costs, possibly recover the initial amount invested and allow for expansion. The Bangladeshi economist tends to use the word "surplus" to make a distinction between the overplus required for a commercially viable social business and the profits earned by conventional companies. Business success in social business should be measured by the contribution an entrepreneur makes to human welfare as opposed to using money as a measure of business success for profit-maximizing companies. With reference to ownership and profit-distribution YUNUS (2010a) distinguishes two types of social business.

<table>
<tr><th colspan="3">Table 1: Two Types of (Grameen) Social Business</th></tr>
<tr><td></td><td>Type 1: Non-loss, non-dividend company with a primary social purpose</td><td>Type 2: Profit-maximizing company owned by its poor (or otherwise disadvantaged) target beneficiaries</td></tr>
<tr><td>Purpose</td><td colspan="2">• Overcoming poverty (or addressing any other problem that threatens people and society) in a self-sustaining way</td></tr>
<tr><td>Ownership</td><td>• Investors (who seek social return on investment rather than financial reward)</td><td>• Target beneficiaries (directly or through a trust that is dedicated to a social cause)</td></tr>
<tr><td>Social Business Model</td><td>• Non-loss making
• Creation of social benefit through the nature of the products, services and / or operating systems</td><td>• Profit maximizing
• Creation of social benefit through the ownership structure
• Product or service might or might not create additional benefits</td></tr>
<tr><td>Profit Regulation</td><td>• No dividend is given to investors beyond the return of the original investment
• When the investment amount is paid back, profits stay within the company for expansion and improvement</td><td>• All profits are to be distributed to the poor (or otherwise disadvantaged) owners or go to a trust that dedicates the profits to a predefined social cause (e.g., community development)</td></tr>
<tr><td colspan="3">Source: Own draft based on Yunus (2007a, 2010a)</td></tr>
</table>

In a **Type 1** social business, it is the nature of the products, services, and / or the company's operating systems that create the social benefit. This kind of social business might, for example, provide food, housing, healthcare, education, or other goods to help the poor or disadvantaged. Once the initial amount invested is paid back to the investor (over an agreed-on time), all further profits have to be reinvested to expand the company's outreach and improve the quality of its products or services in terms of value for money. Profits are, thus, ultimately passed on to the target beneficiaries in terms of lower price, better service, or greater accessibility (YUNUS et al. 2010).

> "Any business that can achieve objectives like these while covering its costs through the sales of goods or services *and* pays no financial dividend to its owners can be classified as a social business" (YUNUS 2007a: 29).

In a **Type 2** social business, the social benefit comes from its ownership structure, while goods or services produced might or might not create additional social benefit. Because ownership of the business is assigned to the poor or disadvantaged (as defined by specific, transparent criteria developed and enforced by the company directors) or a dedicated trust, any financial profits generated by the company's operations should benefit those in need. Theoretically, a social business can also combine both forms of benefits as the Grameen Bank does.

When promoting his idea to the general public, Yunus usually concentrates on Type 1, the non-loss, non-dividend company, reverting to seven principles he developed at the 2009 World Economic Forum in Davos in collaboration with Hans Reitz, Director of the Grameen Creative Lab in Germany (see Table 2).

Table 2: Seven Principles in (Grameen) Social Business Type 1	
1.	The business objective is to overcome poverty or one or more problems (such as education, health, technology access, and environment) that threaten people and society – not to maximize profit.
2.	The company will attain financial and economic sustainability.
3.	Investors get back only their investment amount. No dividend is given beyond the return of the original investment.
4.	When the investment amount is paid back, profits stay with the company for expansion and improvement.
5.	The company will be environmentally conscious.
6.	The workforce gets a market wage with better-than-standard working conditions.
7.	Do it with joy!!!
Source: Yunus (2010: 3)	

Together, these principles are supposed to be "a constant reminder of the values that are at the heart of the social business idea" (YUNUS 2010a: 3). Crucial in Yunus' concept is to explicitly define social business as **excluding the pursuit of individual profit** by investors (at least those owning shares), thus turning the deliberate abdication of personal financial gain by those who invest their time and / or capital into a clear line of demarcation between (Grameen) social business and any other for-profit venture. According to YUNUS (2010a: 2), "any increase in the money going to investors beyond the original investment disqualifies the business from being a social business." This even applies to an adjustment for inflation.

There are three reasons why he regards the total abdication of personal financial gain as important. The first argument is a **moral** one, claiming that it's immoral to make profits to the cost of the disadvantaged. The second argument is **pragmatic:** mixed objectives involve conflicts of interests in business planning, whereas decisions in a social business could be measured against a single yardstick (i.e., the desired social benefit). Otherwise, profit would always trump social or environmental objectives, particularly in times of economic stress. The third rationale is **systemic:** Yunus wants to establish social business as a distinctive alternative, separate from traditional profit-maximizing business and non-profits or rather charities. Even a small dividend could negatively affect the strength of mental commitment. Total delinking from personal financial gain was essential to change mindsets, reshape economic structures, and encourage new thinking (YUNUS 2010a: 14-16).

Practical Considerations

Yunus' expectations are high: once social business became an integral part of the economic structure, it could turn into the "most effective institutional mechanism for resolving poverty" (YUNUS 2010a: 199). Whether healthcare, information technology, education, renewable energy supply, or financial services for the poor, the main challenge was to innovate business models and apply them to produce the desired social results cost-effectively and efficiently (YUNUS 2006a). With respect to the **financial resources** needed to develop and implement social business companies, Yunus counts on capital that currently goes to support philanthropy: "People will invest in a social business for the same kind of personal satisfaction that they can get from philanthropy" (YUNUS 2007a: 25). But due to its self-sustaining character and the fact that investors could get back their money (thus allowing for additional investments), social business would offer more benefits.

Other capital sources were linked to government funds traditionally spent on social programs or CSR budgets of for-profit companies eager to explore new markets. Recent developments support his predictions: since Group Danone set up its Danone Communities fund in 2007, additional investment funds are being set up to provide equity and loan support to social businesses. The initial target for the Yunus Monaco Fund, a joint venture between the Yunus Centre and the Monaco Venture Capital and Private Equity Association, is at around US$ 100 million. The Islamic Development Bank in Jeddah (Saudi Arabia) has announced plans to launch a fund with an initial investment of more than US$ 10 million, while another fund is being planned in Germany. In the long run, specific social stock markets could focus on raising investment capital for social business companies and facilitating the trade of their shares (YUNUS 2007a, 2010a: 168-172).

> "We will need to create rating agencies, standardization of terminology, (…) impact measurement tools, reporting formats, and new financial publications, such as, 'The Social Wall Street Journal'. Business schools will offer (…) management degrees on social business to train young managers how to manage social business enterprises in the most efficient manner" (YUNUS 2006a: 4).

Following Yunus, a driving force behind the creation of new social businesses companies will be human idealism. Soon the **educational system** would adjust to the multidimensional reality of human nature, teaching students a new kind of economic theory that involves both traditional profit-maximizing and social business, thus inspiring them to create their own companies to address challenges ranging from unemployment, health and sanitation to pollution, demographic change and crime. A recent boom in the creation of academic social business chairs and institutes in Asia, Europe, and North America supports this prediction (see Outlook in Section 10.6).

In order to demonstrate the practical feasibility of his concept, Yunus started to create a series of companies that are consciously designed according to his principles. With reference to replications of the micro-credit model, the economist acts on the assumption that once viable prototypes have been developed, they could be replicated all across the globe. Since a social business company operates free from the pressure of earning profit for the owners, the scope of **investment opportunities** would be greater than with profit-maximizing companies. Arguing that profit-maximizing companies needed to assure a minimum financial return on investment, social businesses could theoretically go down to a near-zero profit level, thus involving new options in product and service provision or job creation (YUNUS 2009b: 7). With respect to setting up a supportive infrastructure, Yunus emphasizes the role of governments in giving legal recognition to social business and creating regulatory bodies to ensure transparency in the sector (YUNUS 2009b, 2010a).

Interim Findings (Section 2.1)

- Due to its **normative** nature social business is a highly political term.
- Being composed of **two broad terms**, “social business” as an expression is neither proprietary nor as concise as “micro-credit,” but Yunus believes it represents the evolution of his **old idea** in a new direction. In order to be precise, the research at hand will revert to (Grameen) social business whenever referring to Yunus’ concept.
- Though essentially promoting a new type of **cause** (rather than profit-driven) business, Yunus’ concept also involves a macroeconomic dimension – a critique of shareholder value driven capitalism.
- Yunus distinguishes two types of social business: type 1 is a non-loss, non-dividend company with a social purpose, type 2 a profit-maximizing company owned by its (poor or otherwise disadvantaged) target beneficiaries or a dedicated trust. His call for investors’ total **abdication of personal financial gain** in social business has several reasons, but is primarily to promote a distinctive alternative separate from traditional profit-maximizing business and non-profit organizations.