

Governance and Social Business: The Mutual Benefit of Government's Engagement in Social Business

Muhammad Mustafizur Rahaman and Hisaki Kono

Abstract— Social business drew increasing attention as a mean of achieving economic and social development in emerging economies. While Milton Friedman's doctrine underscores profit maximization as a core business principle, social business addresses social problems at the expense of profit. Practical experience shows that social business encounters a number of problems that hinders its growth. This paper argues that government can boost up and engage in social business in a number of ways. First, social business lacks legal recognition. Government can give it a legal footing. Second, government can provide tax incentive and initial flow of capital for a new social business. Third, in partnership with a private enterprise, government can invest in social business. Finally, government can align foreign aid and social business to make aid more effective. Government's engagement in social business will be beneficial for both. By incorporating social business in its development agenda, government will likely to be able to achieve policy outcome more effectively.

Keywords—Governance, mutual benefit, social business, social problem.

I. INTRODUCTION

SOCIAL business has drawn increasing attention as a mean of achieving economic and social development in many emerging economies. In contrast to Milton Friedman's argument that the only social responsibility of business is to maximize its profit [1], Nobel Laureate Muhammad Yunus coined and popularized the concept of social business [2], which calls for addressing social problems at the expense of profit. This concept, however, is not new and there is a long history of the argument on social enterprises, which apply business strategies to solve social problems and maximize improvements in human and environmental well-being rather than maximizing profits, around the world. The definition of the social enterprises varies across countries depending on its history, and Yunus's argument of social business can be regarded as one of such movements. On the other hand,

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Proponents of market solutions to social problems argue that in a properly structured and sufficiently competitive market, a focus on profit maximization may be the most direct way to contribute to the social good [3]. For example, Porter and Kramer proposed a concept of creating shared value, arguing that social needs as well as conventional economic needs define markets and addressing social problems do not contradict with profit maximization [4]. However, markets respond to the purchasing power, and the poor lack the very purchasing parity, which places profit maximizing business in unfavorable to address the problem of poverty. While increasing number of companies invest in the bottom-of-the-pyramid market, their outreach is in general limited to relatively better-off people. In contrast, the target of most social businesses in poor countries are these unreached poor people.

Yunus calls for governmental role in making a separate legislation for social business and boosting it up. While there is a substantial agreement that government should play a vital role there, but there is much less agreement about how to do it. For example, Yunus argues that government can pass legislation, create regulatory body, and provide tax incentives for boosting social business, in one hand, disagrees with tax exemption, on the other [1]. Contemporary literature also fall short of providing a clear path for governmental role [5]. This research intends to fill that void. With this aim, this research, at the outset, briefly describes the concept of social business. It then gives ground realities of social business implemented in Bangladesh. The proceeding sections show how government can engage in social business and both social business and government be benefited mutually.

II. SOCIAL BUSINESS: DEFINITION, PRINCIPLES, AND DIFFERENCE WITH CONVENTIONAL BUSINESS

This section elaborates upon social business including its definition and core principles. It also highlights how social business differs from Corporate Social Responsibility (CSR) and conventional business.

Yunus describes social business as "selfless" business whose purpose is to bring an end to a social problem, such as, education, health, technology access, and environment [2]. He architects seven principles of social business as follows:

1. business objective is to solve poverty and other social problems rather than to maximize profit;
2. business attains financial and economic sustainability;
3. investors get back their investment amount only. No dividend is given beyond investment money;

4. Profit is reinvested for the expansion and improvement;
5. business is environmentally conscious;
6. workforce gets market wage with better working conditions; and
7. do it with joy.

However, Yunus's definition is not without its limitation. It excludes many for-profit businesses which serves humanities most pressing needs. Given this limitation, Social Enterprise Alliance (SEA) in the United States defines social enterprises as follows in a way that the definition encompasses for-profit organizations whose driving purpose is social [6]:

- a) It directly addresses an intractable social need and serves the common good, either through its products and services or through the number of disadvantaged people it employs.
- b) Its commercial activity is a strong revenue driver, whether a significant earned income stream within a nonprofit's mixed revenue portfolio, or a for profit Enterprise.
- c) The common good is its primary purpose, literally "baked into" the organization's DNA, and trumping all others.

Actually, not all the social business can succeed and some business will eventually incur losses. In that case, the investors will lose their money. If no dividend is allowed as in Yunus's definition, then expected profit from investing in social business is negative, which will discourage potential social investors from investing in social business. Hence Yunus's requirement of no dividend is too restrictive and might probably be harmful. Without this requirement, Yunus's definition is quite similar to SEA's definition of social enterprise. In the following, we do not require no dividend for social business, and we use social business interchangeably with social enterprises.

Social business have emerged in developing countries relatively early. International Development Enterprises (IDE), founded by Paul Polak in 1982, has facilitated local manufacture and distribution of scalable micro-irrigation and low-cost water recovery system for small farmers throughout the developing world at an affordable price. UrmulMarusthaliBunkarVikas (UMBVS), founded in 1991 in India, helped weavers in Rajasthan improve their traditional design and provide them with sustainable livelihood. Another business model which targets at poverty is Base of the Pyramid (BOP) business inspired by Prahalad [7]. For example, mobile phone companies have made cellular phone available to the poor people at affordable prices in many developing countries, which have had a great impact on the lives of the poor. If the objective of the company was to provide the poor with access to telephone network at affordable prices and set the price lower than the profit-maximizing price, then we can regard it as social business.

Around the same time as the growth of social business, profit oriented businesses started catering balance between profitability and social welfare through Corporate Social Responsibility (CSR) activities [8, 9]. According to Carroll's model, a dominant approach to CSR, philanthropic activities by business organizations are desired [10]. Nevertheless, three domain model of CSR by Schwartz and Carroll proposes that doing well for the society is the ethical responsibility of the business organizations [11]. By asking for sacrificing profits for resolving social problems voluntarily, it has some similarity to social business. However, CSR typically devotes a small

portion of profit to the activities and the activities themselves do not have to be financially sustainable. It also implemented as a part of the companies' core business strategies.

Further, in the two dominant models of CSR, proposed by Carroll, Schwartz and Carroll, profit maximization is the first and foremost responsibility of a business organization, on the contrary, addressing social problem is the primary responsibility of a social business organization. A social business is a means of solving social problems whereas a conventional business is a means of earning profits and CSR activities solves social problems by devoting profits earned somewhere else within the companies' business core strategies.

III. SOCIAL BUSINESS FROM THE FIELD: GROUND REALITIES

Yunus implemented a number of social business projects in Bangladesh as a joint venture. Grameen Danone Foods (GDF) Limited and Grameen Veolia Water (GVW) Limited are some of the notable social businesses. This section provides a cursory description about the projects to show the way these are operated in reality.

In order to address malnutrition, which is a common problem among poor children in Bangladesh, Yunus launched GDF, his first joint venture social business, in 2006 with French Danone Company and Grameen Bank holding equal share of capital investment. The main objective of GDF was to alleviate malnutrition among children by providing fortified yoghurt at an affordable price and alleviate poverty through creation of job for the poor families as well as achieve financial sustainability. In order to run the business, the company were obliged to register under the Companies Act 1994.

Bogra, one of the poverty stricken districts in Bangladesh, were chosen to set up the industry and initial cost was US\$1 million. The factory produces yoghurt called "Shoktidoi" from cow milk and date molasses enriched with some food nutrients necessary for children's growth. Farmers having around five cows were chosen to purchase cow milk from. In order to ensure the supply of raw material that is cow milk, Grameen Bank offers loans to potential owners of dairy cattle.

Initially the GDF produced 80 gram yoghurt cup which was priced only at 6 BDT (Bangladesh Taka, equivalent to US\$ 0.06) to make it affordable to the poor children. In order to generate income earning opportunities and address rural poverty, the project employed rural women for door-to-door sales. Grameen ladies, taking loans from the Grameen Bank, buy the Shoktidoi and sell it throughout the villages and receive commissions for each yoghurt they sell. Yunus argues that grameen ladies can reach 200 households per day. However, the sales amount in the first half of year 2007 fell short of the expectation and GDF was not operationally profitable [12]. In order to be financially sustainable, the GDF started selling the product in towns and provincial cities as well with higher prices.

The second social business project was established in 2008, called Grameen Veolia Water (GVW) Limited under The Companies Act 1994 at Goalhari village of Daudkandi Upazilla (a sub-district) under the district of Comilla. The GVW was also a joint venture between French Veolia Water

Limited and Grameen Bank where each party shared for investment of 5,00,000 euro equally [13].

The project set up a water treatment plant near Meghna River. Collecting water from the river, GVW purifies it and supplies it to the village people through a pipeline where 11 communal tap points are established. The Grameen Bank borrowers sell the water to the village people through these tap points and they receive a commission from the selling. Currently, the project also install water supply points at the house by the cost of the water consumers.

Considering the poverty of the area and social business principle, the project provides 10 liter pure water only with 2.5 BDT to rural areas. The project started its business at Goalmar in 2009, then Padua in 2010. Now the project provides safe drinking water in six villages in two Union (the lowest tier of local government). Total beneficiaries include seven hundred families' and teachers and students of two schools account for roughly six hundred consumers. Sales volume in the rural area is around 5000 liter per day. By selling water with such a low price, the project suffered from losses. In order to recover the company's capital investment and operating expenses, the GVW started selling water in urban areas, where it sells 20 liter Jar water in 70 BDT. Presently urban sales constitute approximately 500 jars per day in about 300 organizations.

In these two cases, GDF and GVW sell the same products at much higher prices in cities to compensate losses in rural areas. The beauty of the financial sustainability in the original definition of social business is that it enables the programs to expand without budget limitation because the program is financially self-sustained and the program size is not constrained by the fund availability. But in these two programs, the program in rural areas itself is not financially sustainable, which forced them to sell the same product at higher prices in urban areas. Then the expandability of the programs is confined by the profit earned in urban areas and they look more like CSR activities than social business in the sense that they depend on profits earned somewhere else.

Given the difficulty confronted by many social businesses, it will not be unwise to propose for governmental role in boosting up and rescuing the business where necessary. Governments will have four ways to boost up social business, including mandating, facilitating, partnering, and aligning aid with social business.

IV. MANDATING SOCIAL BUSINESS BY GOVERNMENT

Mandating herewith refers to making legislation. Social business has no legal footing in many developing countries as there is no separate laws and regulations for it. Government can create a separate law or incorporate some sections in the existing company Laws. This sections attempts to provide some suggestions for regulatory law for social business.

Countries around the world have different Act and Rules of permitting various types of organizations or firms or associations. In many countries where the idea of social enterprises or social business is still new, there is no separate laws and regulations specified for social business. For example, in Bangladesh, Any business irrespective of "for profit" or "not for profit" must be registered under The Companies Act 1994

and be filled up the necessary requirements set by the Act [14]. A business oriented company has no scope for getting registration under NGO or cooperative rules while whereas the Act provides no specific regulations for social business. Government can draft a separate legislation or incorporate some sections in the existing laws. The Companies Act 2013 of India is a good example in this regard. Section 135 of the Act requires that companies having certain amount of net worth or profit are required to spend 2% of their profits in the CSR activities, and Schedule VII of the Act identifies 10 areas of the CSR activities, one of which is the social business project [15]. Specifying social business in the law is a minimum legal basis of a social business, and much more will be needed to boost it up. Many company acts have a section on types or modes of companies, where social business can be incorporated and defined clearly. Without separate regulations, social business is subject to the same regulation as the conventional profit-maximizing companies, which makes it difficult to encourage social business which aims to improve social welfare, whose objective is much closer to the government's interest.

V. FACILITATING SOCIAL BUSINESS BY GOVERNMENT

Facilitating means boosting up through injecting financial and non-financial incentives. This section finds out how government can provide incentives for social business investment.

To keep up the balance between social impacts and financial sustainability puts the business at the crux of the situation. Guaranteeing flow of finance is the most important factor for sustenance of a social business project [16]. Coupled with price hike in petroleum, bad monsoons caused an increase in milk prices between 2007 and 2008 for which GDF reduced the quantity of the yoghurt and increased price per cup of yoghurt in 2008 [17]. Similarly, GVW turned to profit seeking business partially to recover its loss [18]. The financial deficit generated in rural areas constrains the expansion of the business.

Government can facilitate social business by creating conducive framework for fiscal matters. Several examples can be cited here. The Government of Bangladesh (GOB) declared 10% tax rebate for CSR practice. Any company will get exemption of Income Tax at the rate of 10% for actual cost in CSR. The GOB also provides various monetary and non-monetary facilities for attracting investment in the Export Processing Zones (EPZs). Investors in the EPZs were likely to get 10 years tax holiday, duty free import of construction materials, machineries and equipment's, duty free export of raw materials and finished goods, secured land, off-shore banking and back to back L/C, and enjoy most favored nation status. NGO or cooperative rules also provide tax rebate in some cases. Similar provisions could be made for social business to make it easier to be financially sustainable. Government can also provide financial resource through creating a fund. The Companies Act 2013 of India provides scope for companies to donate in the fund as a part of their CSR activities. Likewise, a special fund may be created by the government by its own fund and receiving donations from business organizations. Government can use the fund to cover

part of the set-up cost for social business which is selected through kind of social business competition.

VI. PARTNERING WITH PRIVATE ORGANIZATIONS BY GOVERNMENT

Partnering means working jointly. This section provides opportunities for the government to engage in social business in partnership with private enterprises.

Government is ultimately responsible for solving social problems. Partnership with social business might enable the government to discharge its responsibility more efficiently. In Tirpur, a small town of southwestern Tamil Nadu, industries and local residence suffered from scarcity of pure water due to heavy pollution in the ground water. Realizing the insufficient capacity of old state funding scheme, the Government of Tamil Nadu formed a company called "New Tirpur Area Development Corporation Ltd" with support from experienced financing, engineering and construction companies. The new company then signed a thirty year concession with the government with an expected return on investment of 20%. The benefits of the project were multifold. First, the project installed 8000 new connections of water supply. Second, prior to the project the Tirpur municipality supplied water once every three to four days, after the project, it was every other day. Third, in the slums water was supposed to supply free of cost. The project was able to reduce monthly water tariff from 350 to 85 Indian Rupee per month [19]. This is a good example of private and public partnership for producing public good with an affordable rate.

Public private partnership in social business differs from conventional business by its purpose and target beneficiary. For example, the purpose of the Tirpur Area Development Project was to supply pure water to the local residence at an affordable cost. Conversely, Yamuna Expressway, the largest public-private partnership project that made a link between Delhi and Agra is used mostly by higher income people. Moreover, the same partnership might differ in getting return of the investment. The internal rate of return (IRR) of a conventional business may be higher than that of a social business.

VII. ALIGNING FOREIGN AID WITH SOCIAL BUSINESS BY GOVERNMENT

Foreign aid has a long history of producing fewer than expected benefits. Social business has widened new opportunity of making aid effective through market mechanism. This section focuses on aid alignment with social business.

Developing countries have depended on assistance from the aid donors to minimize the gap between aspirations and resources. Most of the African Countries cannot fulfill half of their total budgetary commitments without foreign aid [20]. In Bangladesh, 39% of the Development Budget of 2012-13 dependent on foreign aid [21]. But its effectiveness on development and poverty alleviation in the recipient countries

remain a subject of heated debate. Easterly critically examined the role of foreign aid worldwide and found that foreign aid generally has a poor record in eradicating poverty [22]. A World Bank Study report reveals that foreign aid in different times and different places has thus been highly effective, totally ineffective, and everything between [23]. Question also arises whether aid money effectively reaches to the poor. Rahaman found that foreign aid benefits key politicians, policymakers and bureaucrats at the expense of those who are the intended beneficiaries [24].

In pursuit of the effectiveness of aid, the international donors began discussing aid effectiveness from the late 1990s, focusing on better harmonization [25]. The latest OECD evaluation, however, concludes that burdens of aid management in the recipient countries have not reduced much, and alignment and harmonization progressed more unevenly [26]. In Bangladesh, a large number of aid donors and NGOs are working but most often, they work without coordination and overlaps each other. Such uncoordinated activities may have the chance to overflow of services in one area while making the services scarce for other areas.

To facilitate coordination, governments and aid donors work together to write development policy papers. Once they can identify which sectors are well suited for aid programs and which sectors have potential for social business development, they can include social business in the development policy papers. Moreover, a new LCG (Local Consultative Group) committee can be created with representatives from the government, aid donors, and social business. The responsibility of the LCG will be to share the issues they are facing and to facilitate further cooperation between them for proceeding the development policy in more harmonized and efficient way.

It is noteworthy that all sectors is neither feasible nor required for social business investment. Further research is necessary to identify which sectors are good for social business.

VIII. CONCLUSION

Social business intend to solve social problems rather than maximize profit. Sacrificing profit, the business struggles for its sustainability. The GDF and GVW earned profits in urban areas in order to subsidize the loss in rural areas. Though Yunus categorize them as social business, the programs in rural areas, which are their main target, are not financially sustainable and depend on the profit generated somewhere else, making the programs much more like CSR. Because both business registered under The Companies Act 1994 in the absence of a separate legislation, they got no tax exemption or financial benefit which might have been useful to make the programs more financially sustainable at least to some extent. Governments can play roles in boosting up social business by formulating legislation, providing financial incentives for social business, implementing social business project in partnership with the private sector, and above all aligning aid with social business. Government's engagement will hasten the flourishing of social business in one hand, and help government to achieve policy outcomes effectively on the other.

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