Failing to Scale and Scaling to Fail: How Social Entrepreneurs Exploit Impure Non-profits in Order to Attain Economies of Scale

Andrew Isaak[1]

[1]PhD Student, University of Mannheim, Germany: Institute for SME Research & Entrepreneurship

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The sharing economy, as exemplified by firms such as AirBnB, Couchsurfing and BlaBlaCar, attracts researchers from diverse disciplines and largely falls into the category of social entrepreneurship. Sharing businesses are said to make better use of idle resources, to allow individuals to earn higher rents (i.e. on their flat or car) and to have a largely positive effect on the environment in terms of waste reduction (Benkler, 2004, Botsman and Rogers, 2011, John, 2013, Belk, 2014a, 2014b). On the other hand, most sharing firms are clearly for-profit enterprises, often with astronomical valuations (as in the case of Uber, the controversial private ride firm).

The discussion of the sharing economy is still at an early stage, where questions often center on definitional aspects (such as scoping the field or denoting preliminary typologies) or on motivations to engage in the sharing economy (the demand side). Schor (2014) dichotomizes the sharing economy into for-profit and non-profit business models as well as into business-to-peer (B2P) and peer-to-peer (P2P) forms. Motivations for participation have been primarily examined in the car-sharing industry and can be loosely grouped into cost savings, service benefits, the reduction of the burdens of ownership and environmental concerns (Burkhardt and Millard-Ball, 2006).

This paper examines the supply side and more specifically which business models (Osterwalder et al, 2005; Zott and Amit, 2009) fail to scale in their respective industry and geographical contexts, starting with a null hypothesis that purely non-profit business models fail regardless of industry or phase of economic development (according to the categories of the Global Entrepreneurship Monitor, see Amóros, Moska and Singer, 2015).

Since sharing firms rely on online network platforms and diffusion of their brand name (or service innovation), they need to reach a critical mass of users fairly quickly. As the market for sharing has low barriers to entry, competitors can emerge suddenly and existing startups need to step up or out. Stepping up requires significant cash flow to finance advertising, marketing and promotion, which non-profit firms are unlikely to have unless, conceivably, backed by a wealthy donor over a considerable period of time.

A counter example is Wikipedia – a non-profit that has unarguably reached a global scale – wherever internet access is possible. This raises the question what allowed Wikipedia to succeed where others have failed. Wikipedia can be seen as originating in an Anglo-Saxon, democratic and entrepreneurial culture characteristic of the United States, which scores highly on total early-stage entrepreneurial activity, media attention for and status of entrepreneurship, entrepreneurial intention, perceived opportunities and capabilities as well as cultural and social norms (i.e. the extent to which norms encourage or allow new business: Amóros, Moska and Singer, 2014). While Wikipedia demonstrates that it is possible to scale and sustain a non-profit sharing venture, the business model is unique to knowledge sharing, with comparatively low transaction costs when compared to physical goods (Williamson, 1981). Conceptually, the costs of Wikipedia's business model can be reduced largely to hosting and administration expenses.

A smaller example, arguably a part of the sharing economy, is betterplace.org – a donation-based crowdfunding site based in Berlin and operated by the non-profit company gut.org gAG. Crowdfunding is often identified as a facilitator of social enterprises whether or not it is strictly 'social', philanthropic or a mixed 'blend' form of venture capital (Belleflamme, 2014).

However, two things are observable in the case of betterplace.org:

(1) the organizational form gAG is a blend of the public stock corporation and a non-profit firm, i.e. the business is an 'impure non-profit' and

(2) donation-based crowdfunding is at the fringe of what is typically considered sharing.

Two other cases are notable – startnext.org and crowdsurfing.com

Startnext, the largest German crowdfunding platform, started as a non-profit firm (Startnext gUG/small non-profit form) in 2010 and converted to for-profit (GmbH/limited liability corporation) a year later. When social entrepreneurs give up on non-profit business models they compromise or corrupt their ideals and vision or "scale to fail".

Similarly, couchsurfing.org is run as a for-profit enterprise (Couchsurfing International, Inc., a type B corporation). To be fair, *benefit corporations* are required to have a social mission in addition to profit maximization and can thus be seen as an 'impure' non-profit. Type B corporations began emerging in 2010 and are therefore a novel phenomenon.

Thus (nascent) social entrepreneurs in the sharing economy are faced with a dilemma – failing to scale (by sticking to 'pure' non-profit business models) or scaling to fail (not in an economic sense, but in the sense of compromising their ideals by choosing a for-profit or mixed, 'impure' non-profit organizational form that is more likely to attract outside capital). Further, it seems likely that necessity-driven social (sharing) entrepreneurs in factor-driven and efficiency-driven countries are likely to make different choices here than their counterparts in often wealthier, innovation-driven countries, which more often have the luxury of focusing on business sophistication (Amóros, Moska and Singer, 2014).

Based on a discussion of these phenomena, a framework is developed that delineates a set of criteria that can be used to predict firm failure (and possibly sustainability) for non-profits in the sharing economy. In addition a second set of criteria facilitate measuring scalability of the sharing business model, accounting for the host country's phase of economic development (based on the GEM 2014 indicators). It can be concluded that the initial null hypothesis, that non-profit firms always fail in all industry contexts is to be rejected. An alternative hypothesis is proposed, excluding the knowledge-sharing industry.

This paper contributes to the emerging research stream on the sharing economy, but also to social entrepreneurship theory and the business model scalability debate. Practical implications include facilitating the social entrepreneur's decision as to which organizational form and business model to choose in the sharing economy depending on the industry in question in order to achieve scalability or fill a niche.

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