Striking the right balance
Views from Charity and Social Organisation CEOs
The environment in which social enterprises operate is changing rapidly. To better understand the range of challenges they face today, we held a series of in-depth interviews with chief executives, who provided fascinating insight into issues ranging from competition to diversification.

There are approximately 70,000 social enterprises in the UK 1, running everything from banks to children’s services and pubs to leisure centres. What separates them from other organisations is that they reinvest the money they make back into their businesses and local communities. Uniting them is a clear social or environmental mission at the heart of their governing documents.

Any organisation that has developed to become a social enterprise will have encountered bumps along the way. In the current climate of on-going austerity and political uncertainty, social enterprises are also having to adapt to harsh economic realities.

Local authorities are tightening their belts as never before, and many of our interviewees have been hit hard by the scale of this cost-cutting, and the impact it has had on their organisations.

One CEO we spoke to said local authority pricing had been “cut to the bone”, and raised concerns about the impact this could have on the service residents receive.

At the same time, competition for public sector work has never been fiercer, and some social enterprises have found it too much of a struggle vying with asset-rich private sector providers for local authority work.

One CEO we spoke to described how their organisation is preparing to shed two-thirds of its workforce after losing a single local authority contract.

Organisations are now recognising the dangers of being too reliant on any one source of revenue, and are responding by adopting an increasingly commercial mindset in order to diversify and seek out new revenue streams.

One CEO commented that by taking such an approach, there is always a danger that organisations can lose sight of their social purpose as they “follow the money”.

Indeed, there was a clear sense from our interviews that a growing number of social enterprises are asking themselves the question: “What are we for?”

There is also a sense, however, that social enterprises are learning from their experiences, and are increasingly aware of what it will take to adjust to the environment they now find themselves in. They are learning to be bold, innovative and resilient as they explore new opportunities and potential revenue streams.

1. https://www.socialenterprise.org.uk/Pages/FAQs/Category/FAQs
Leaders of social enterprises are regularly faced with challenging strategic decisions: what business model to adopt, which revenue streams to seek out, and how to attract, train and retain the right staff and volunteers.

One of the clearest themes to emerge from our interviews was that organisations are increasingly having to contend with factors which might reasonably be described as being outside their sphere of influence.

Austerity
The shadow of austerity, for instance, has loomed large over the charitable sector for a number of years. Between 2008 and 2014, it is estimated small and medium-sized charities saw their income fall by around 17%, while a report last year found two-thirds of charities are seeing increasing demand for their services.

One interviewee told us that financial pressures being placed on local authorities are leading to "robust conversations with commissioners" about what service provision needs to be dropped as a result of the imposed savings.

But there are other emerging risks that are keeping CEOs awake at night.

Data security
Data security is one such risk. Social enterprises are responsible for processing vast quantities of personal data about their staff and customers, and data breaches are all too common. The Information Commissioner’s Office investigated 120 alleged data breaches involving voluntary sector organisations in 2016.

It was clear from our interviews that the burden of ensuring personal data doesn’t fall into the wrong hands is weighing heavily on some.

One leader said their organisation was considering outsourcing their data storage, but was worried about whether or not it would be handled safely.

“We have to protect personal data but first we need to understand what we hold and where we keep it,” said this CEO. “Until we have reviewed and fixed our processes, we are not going to invest heavily in IT, otherwise we are in danger of just making a broken process faster.”

Brexit
Britain’s impending exit from the European Union is another emerging risk.

Surveys ahead of the EU Referendum last June found three-quarters of social enterprise leaders wanted to remain in the EU, although most were confident Brexit would not put their businesses at risk.

After the Referendum, Peter Holbrook, Chief Executive of Social Enterprise UK, warned: “There is no blueprint for Brexit. No country has ever left the EU, so we have no real idea just how bumpy a ride the economy is in for.”

What was clear from our interviews, however, is that Brexit is already having an impact when it comes to staff recruitment and retention.

One CEO said: “We were totally caught out by the result of the EU referendum. I don’t think anybody really expected that to happen. The sooner the government decides what the status of EU nationals will be after Brexit, the better, as people are already starting to leave because they are concerned about what is going to happen to them.”

Another leader said: “We’ve already lost three members of staff as a consequence of Brexit. They’ve gone to Germany because they no longer feel comfortable here.”

Regulation
Onerous regulations are also making it harder to recruit and retain staff in certain sectors. One of the CEOs we spoke to, who leads a childcare enterprise, said: “We get squeezed by government policy decisions which create barriers. An example is the requirement for minimum educational standards for those seeking to do Level 3 nursery supervision. It’s led to a 96% drop in apprentices, which is a major issue for us.”

Addressing these complex challenges necessitates taking innovative approaches and bold decisions. This childcare enterprise, for example, is looking to address its recruitment gap by employing more older staff.

“We’ve made contact with a major private sector firm to understand how they employ older people so we can find it out if it could be an option for us,” said this CEO.

2. https://goo.gl/l6uwp
How costs are being “cut to the bone”

As local authorities tighten their purse strings ever further, social enterprise CEOs are fearful about the impact on service provision.

With so many social enterprises dependent on public sector business, the extent to which local authorities are now focusing on price when awarding contracts has become a real concern.

One CEO said that while their organisation generally scores well on the ‘quality’ metrics that councils use as part of their tender processes, these quality metrics are usually given a lower weighting than price.

They said: “Decisions are hugely based on price – sometimes it’s as much as 80% price and 20% quality”. They also offered this stark warning: “There has to be a concern about the governance and safety of some of these deals.”

Cut-to-the-bone pricing must be a risk to residents.”

Some social enterprises are also finding themselves in competition with local authorities.

One CEO of a childcare enterprise described how it was being undercut by councils that are opening up cheaper nurseries.

This CEO said: “Local authorities are becoming both our regulator and competitor. They are locking down the competition, paying the best rates and opening nurseries in the wrong places.”

One social enterprise CFO told us that cost cutting can still have an impact even after contracts have been signed, with some councils “attempting to renegotiate the pricing after the contract has started. Trying to take another 5% off each year.”

In this increasingly competitive world, charities and social enterprises are also realising they can no longer take old norms for granted. Many are finding their business models threatened, both by changing demographics and by the offerings of rival providers.

One leader described their marketplace as getting “nasty”, adding: “There’s intense competition and it is very price focused.”
The dangers of having “all your eggs in one basket”

Organisations are becoming increasingly aware of the risks of being too dependent on any one revenue stream.

“There’s a massive need to transform public service delivery. The old ways aren’t working.”

“You start off trying to change the world, and end up trying to change your job.”

“Charity CEOs don’t talk to each other. Collaboration is key but it’s a struggle.”

“Some organisations ricochet from one funding stream to another, with no stability or security. And somewhere along the way they lose their sense of purpose as they follow the money.”

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Many social enterprises can find themselves in a precarious position when faced with competition from larger providers with greater resources.

The leader of a health and social care enterprise recounted how it had recently lost a major local authority contract it had held for several years, and which accounted for more than half of its business.

Until the loss of this contract, this enterprise had been undergoing a period of sustained expansion, which had seen it double in size in the preceding five years. Now, however, the organisation is likely to have to reduce its staff numbers by two-thirds.

This organisation’s CEO believes IT innovation was a key reason it lost this particular contract. They said: “Our IT system is fairly antiquated, but the business model for social enterprises doesn’t really allow for much capital investment.”

IT was a concern for several of our CEOs. One, who heads a leisure trust, remarked that “IT changes at a pace that is impossible to keep up with”. They also commented that their organisation did not want to invest in IT until they had reviewed and fixed the processes – such as staff training – that might render personal data held on IT systems vulnerable regardless of the technology used.

Despite concern about IT from some of the social enterprises we spoke to, many others recognise the positive changes that technology investment can bring.

One social enterprise CFO told us: “We have to be innovative”, commenting that report writing is already being conducted on iPads, which then push the documentation out to various computer systems.

The experiences of a health and social care provider also highlights other issues faced by many social enterprises, such as:

- Over-dependency on public sector funding and/or a single large contract
- The need to diversify in order to avoid having “all your eggs in one basket”
- Finding partners with the same values when diversifying
- The challenge of responding to public sector procurement criteria

A health and social care CEO explained how when bidding to retain a particular local authority contract, it had emphasised its service quality and delivery model. However, only 7% of the score the local authority used to choose a provider was based on these measures.
Diversification and collaboration is key

With old funding streams “getting tired”, social enterprises are understanding the importance of developing a diversification strategy.

Social enterprises are not meekly surrendering to the challenges they face.

Many are exploring new business models. One interviewee said their organisation was considering a “Robin Hood model”, whereby income generated from commercial activities is used to subsidise services for the most disadvantaged.

Many organisations are also exploring new ways of working.

The most recent State of Social Enterprise Survey6 found around two-thirds of social enterprises are diversifying into new markets.

The importance of diversity

Most of our interviewees agreed on the importance of developing a diversification strategy, however, they were also united in the view that diversifying brings its own set of challenges.

One CEO remarked that diversity has become more important as “old funding streams are getting tired”.

However, there was much discussion about the difficulty in finding a balance between diversifying into new revenue streams and retaining your organisation’s core values and unique selling points.

Another interviewee put it more bluntly: “Some organisations ricochet from one funding stream to another, with no stability or security, and somewhere along the way they lose their sense of purpose as they follow the money.”

Developing a diversification strategy requires a clear understanding at the outset of how far you are prepared to move away from your core services, and the risks and rewards of doing so.

One social enterprise leader recounted how, back in 2014, it decided it would target 30% of its business in non-local authority leisure.

“We are now looking at library services, children’s centres and education programmes for young people,” they said.

While today’s organisations may be willing to consider changing their business appetite in order to exploit commercial opportunities, there are also risk considerations.

For example, some social enterprises have diversified into offering services that include providing expertise or advice, such as employment training or money advice.

Many of these professions are heavily regulated by professional bodies, and there will probably be a requirement that practitioners in these areas hold a minimum level of professional indemnity cover to protect themselves against potential negligence claims.

Collaboration requires a cultural shift

Our interviewees also discussed how collaboration is becoming ever more important.

As one put it: “Collaborative working is the only way to change the world.”

For collaborative working to be effective, both parties have to understand and appreciate what the other can bring to the arrangement.

One CEO commented: “Charity CEOs don’t talk to each other.

“Collaboration is key, but it’s a struggle. Partnership working (including local authorities) is crucial for the way forward but there’s risk involved.

“Small charities are suspicious of larger charities wanting to take over.”

This CEO suggested that moving beyond this mind-set would require a “cultural shift”.

Another interviewee reflected that harsh commercial realities were forcing their social enterprise to consider partnering with another organisation whose values were not necessarily aligned with its own.

Another of our interviewees was adamant that despite the inherent challenges, increasing levels of collaboration were inevitable. “In 10 years’ time, the market will not be able to sustain the same volume of charities doing similar work,” they said.

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Final thought

As social enterprises expand and diversify, some are walking a financial tightrope, while others are asking the question “what kind of organisation do we want to be?”

While social enterprises are becoming bolder than ever before, there is a sense of anxiety about the speed of this transformation, and an awareness that there will be losers as well as winners.

One concluded: “We’re all in a struggle to survive over the next few years. We won’t be talking about ‘commercial mindset charities’ in the future, because it will be the norm. Commercially minded charities will be the only ones left.”

In the short to medium term, there are also concerns over how to finance the transition to a more commercial business model.

One of our CEOs described cash flow as a particular concern, and admitted to feeling nervous about their organisation’s decision to take out a £12m bank loan. But they are by no means alone in taking this path.

The percentage of social enterprises that have sought finance for working capital rose from 28% in 2011 to 43% in 2015, according to Social Enterprise UK.

While the leaders of today's social enterprises may feel some anxiety about having to restructure their business models and seek alternative sources of finance, it is striking how successful most social enterprises have been in overcoming the hurdles they have faced in recent years.

Nearly three-quarters of social enterprises now earn the vast majority of their income from trade – and research suggests they are not only developing more new products and services than private sector SMEs, they are also creating more jobs too.

As social enterprises continue to grow and expand, there is a recognition they need to make the most of what sets them apart from their private sector competitors – their social value.

As one leader put it: “Organisations are happy to work with us, because we are a social enterprise. But what we don’t do enough of is sing from the rooftops about our social enterprise values. “I was looking through a brochure we’d produced and I struggled to find the words ‘social enterprise’ anywhere. The wider perception of what we are for is an important issue.”

Others are still asking themselves the question, ‘what are we for?’

As one leader put it: “We changed our business model five years ago to be a social business, but we are still unsure about the kind of organisation we are.”

From austerity to Brexit to data security concerns, social enterprises are facing unprecedented challenges. In this climate, CEOs need to be innovative, resilient and bold to secure the long-term future of their organisations.

While concerns and anxieties will remain, there are reasons for optimism as social enterprises continue to demonstrate their ability to learn, adapt, diversify and endure.

Zurich Municipal would like to thank the participating social enterprise chief executives who helped make this report possible.