tepsie
growing social innovation

Social Innovation
Context and Responses

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Content

1. Social Innovation in context

The global field of social innovation is gathering momentum, with new institutions, methods and models. There is growing enthusiasm and interest among foundations, policy makers and entrepreneurs. Some regard social innovation as a means of changing the way governments work, some see it as changing the actions of business and others see social innovation as the result of improving the impact and effectiveness of civil society organisations. But what is driving this growing interest in social innovation? Why are philanthropists, businesses and governments putting social innovation firmly on the agenda?

There are a number of seemingly intractable social challenges that existing structures, policies and institutions have failed to address. Issues such as unemployment, marginalisation, child poverty, growing inequalities, addictions, homelessness, crime and criminalisation and low levels of educational attainment amongst vulnerable groups, remain challenges for governments and communities across Europe. New challenges have also emerged over the past few decades. Migration and hyper-diverse communities have put pressure on community cohesion and in some cases, placed additional demands on already pressed local services; a rapidly ageing population has dramatically increased demands on health and care services as well as public and personal budgets; climate change and resource scarcity pose significant challenges to governments and citizens globally and; new lifestyles have brought with them problems of obesity and chronic disease such as diabetes. Chronic disease and demographic shifts are particularly worrying - these trends are set to worsen dramatically over the coming decades and place significant demands on already stretched health and care services.

These growing social, environmental and demographic pressures are challenging the very foundations of the modern welfare state. How will future social needs be met and by whom? The current economic crisis has added urgency to these questions. In the last few years, Europe has suffered the worst financial and economic crisis in decades with record levels of unemployment and public debt and low levels of growth among many Member States and severe contractions in others. These social, environmental and demographic challenges are placing an ever-increasing burden on public spending, at a time when public budgets are already being squeezed. There is also growing awareness that institutions and structures as they are currently constituted are incapable of dealing with the complexity and scale of these challenges. This is the backdrop for the growing calls for greater levels of innovation in thinking how we respond to these social issues.

We argue that the current economic crisis marks a fundamental shift in the nature of our economies. As Robin Murray explains, "it is a crisis of the real economy, of an old form of production and consumption, of its sources of energy and its means of transportation."[1] We argue that this crisis marks a point in the transition from a techno-economic paradigm based on mass production to one that is based on information and communication technologies. The Information Revolution promises to modernise every aspect of society and the economy, and in so doing drive economic growth and societal progress.

This transition has wide ranging implications for social innovation. We need to understand the nature of this change in order to determine what kind of social innovation will be enabled and needed as a result of this paradigm shift. New technologies also shape and change prevailing attitudes and assumptions which in turn play a key role in driving social innovation.

[1] R Murray, *Danger and Opportunity: Crisis and the New Social Economy*, NESTA, London, 2009

1.1. Long waves and new paradigms

Joseph Schumpeter was one of the first economists to see entrepreneurship and technical change as the source of economic growth. The hero in his story was the entrepreneur – the person who unleashes the forces of 'creative destruction' and in so doing drives economic growth. His analysis has been extended and deepened into theories of long waves of economic activity, most notably by Luc Soete, Chris Freeman and Carlota Perez.[2]

Like Schumpeter, Perez sees technical change as the source of economic growth and development. She describes 'great surges of development' which are enabled by paradigm shifting technologies that emerge roughly every 50 years. These technological revolutions can be defined as "a major upheaval of the wealth-creating potential of the economy, opening a vast innovation opportunity space and providing a new set of associated generic technologies, infrastructures and organisational principles that can significantly increase the efficiency and effectiveness of all industries and activities."[3]

1.1.1. Installation and Deployment

According to Perez, each technological revolution has two distinct phases: the period of installation and the period of deployment. The irruption of the technological revolution is followed by two or three decades of Schumpeterian creative destruction, as entrepreneurs join forces with financial capital to take on the established firms and models of the old paradigm. This installation period is a time of intense experimentation and exploration of the possibilities of the new technologies. During this installation period, capital faces declining yields from the mature industries of the previous paradigm. The emerging paradigm offers new opportunities and finance follows the prospects and infrastructures of the new. This phase ends in a major bubble and a crash.

The crash, Perez argues, leads to a brief period of capital devaluation and a re-composition of the socio-institutional frameworks that regulate finance and set the conditions for another phase of economic development. The deployment phase is where the new paradigm is fully established and helps to modernise existing industries, institutions and activities.[4] The period is marked by more organic growth and lasts until maturity and exhaustion are reached, setting the stage for the irruption of the next technological revolution.[5]

Perez states that our current crisis is one such turning point in a technological revolution and the establishment of a new techno-economic paradigm.[6] She argues that we are moving away from an old paradigm based on mass production and into a new paradigm based on information and communication technologies.

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[2] See for example, C Freeman, *The Economics of Industrial Innovation*, Cambridge, MIT Press, 1982; C Freeman, *Technology Policy and Economic Performance: Lessons from Japan*, Pinter Publishers, London, 1987 and; C Freeman, J Clark and L Soete, *Unemployment and Technical Innovation: A Study of Long Waves and Economic Development*, Westport, Greenwood Press, 1982.

[3] C Perez, 'Technological Revolutions and Techno-economic Paradigms,' *TOC/TUT Working paper,* No.20, 2009.

[4] C Perez, 'Technological Revolutions and Techno-economic Paradigms,' *TOC/TUT Working paper,* No.20, 2009.

[5] C Perez, 'The double bubble at the turn of the century: technological roots and structural implications', *Cambridge Journal of Economics*, vol. 33, pp. 779–805, 2009

[6] C Perez, *Technological Revolutions and Financial Capital,* Edward Elgar, 2002; C Perez, 'After the crisis – creative construction', *Open Democracy*, 5th March 2009

Table 1 - Five Great Surges of Development: Main technologies, industries and infra-structures and prevailing techno-economic paradigm7

Technological Revolution	New technologies and new or redefined industries	New or redefined infrastructures	Techno-economic paradigms – 'common sense' innovation principles
FIRST: the 'Industrial Revolution' (1771)[8]	Mechanised cotton industry Wrought iron Machinery	Canals and waterways Turnpike roads Water power (highly improved water wheels)	Factory production Mechanization Productivity/ time keeping and time saving Fluidity of movement (as ideal for machines with water-power and for transport through canals and other waterways Local networks
SECOND: Age of Steam and Railways (1829)	Steam engines and machinery (made in iron; fuelled by coal) Iron and coal mining (now playing a central role in growth) Railway construction Rolling stock production Steam power for many industries (including textiles)	Railways (use of steam engine) Universal postal service Telegraph (mainly nationally along railway lines) Great ports, great depots and worldwide sailing ships City gas	Economics of agglomeration/ Industrial cities National markets Power centres with national networks Scale as progress Standard parts/ machine made machines Energy where needed Interdependent movement (of machines and of means of transport)
THIRD: Age of Steel, Electricity and Heavy Engineering (1875)	Cheap steel (especially Bessemer) Full development of steam engine for steel ships Heavy chemistry and civil engineering Electrical equipment industry Copper and cables Canned and bottled food Paper and packaging	Worldwide shipping in rapid steel steamships (use of Suez Canal) Transcontinental railways (use of cheap steel rails and bolts in standard sizes) Great bridges and tunnels Worldwide Telegraph Telephone (mainly	Giant structures (steel) Economies of scale of plant/ vertical integration Distributed power for industry (electricity) Science as a productive force Worldwide networks and empires (including cartels) Universal standardization Cost accounting for control and efficiency Great scale for world market power/ 'small' is successful, if local

[7] Adapted from C Perez, *The financial crisis and the future of innovation: A view of technical change with the aid of history,* Working Papers in Technology Governance and Economic Dynamics, no. 28, 2010, p5

[8] It is important to note that this table reflects the Great Surges of Development as they occurred in the UK, USA and Germany. Surges of Development have occurred at different times for different countries (in some cases, industrialisation began much later in the 20th Century, surges were far briefer than noted above and in some counties, several surges took place at the same time). The dates above are relevant for the UK, Germany and France and less so for new EU Member States such as Poland, The Czech Republic, Slovakia and Hungary.

		nationally) Electrical networks (for illumination and industrial use)	
FOURTH: Age of Oil, the Automobile and Mass Production (1908)	Mass-produced automobiles Cheap oil and oil fuels Petrochemicals (synthetics) Internal combustion engine for automobiles, transport, tractors, airplanes, war tanks and electricity Home electrical appliances	Networks of roads, high-ways, ports and airports Networks of oil ducts Universal electricity (industry and homes) Worldwide analogue telecommunications (telephone, telex and cable-gram) wire and wireless	Mass production/mass markets Economies of scale (product and market volume)/ horizontal integration Standardisation of products Energy intensity (oil based) Synthetic materials Functional specialisation/hierarchical pyramids Centralisation/metropolitan centres/ urbanisation National powers, world agreements and confrontations
	Refrigerated and frozen foods		
FIFTH: Age of Information and Tele-communications (1971)	The information revolution: cheap microelectronics Computers, software Telecommunications Control instruments Computer-aided biotechnology and new materials	World digital telecommunications (cable, fibre optics, radio and satellite) Internet/ Electronic mail and other e-services Multiple source, flexible use, electricity networks High speed multi-modal physical transport links (by land, air and water)	Information intensity (microelectronics-based ICT) Decentralised integration/ network structures Knowledge as capital/ intangible value added Heterogeneity, diversity, adaptability Segmentation of markets/ proliferation of niches Economies of scope and specialisation combined with scale Globalisation/ interaction between the global and the local Inward and outward cooperation clusters Instant contact and action/ instant global communications

Source: Perez 2010

1.1.2. The new paradigm

The emergence of the new paradigm began in the 1970s with the creation of the Intel microprocessor. This technological revolution – first of calculators and minicomputers, then personal computers, software, telecoms, the Internet and the World Wide Web – gathered pace throughout the 1980s and 1990s. Growing confidence and excitement about the possibilities of new information and communication technologies, together with the prospect of significant capital gains in the stock market, led to the dotcom mania and bubble of the 1990s which burst abruptly in 2000.

Despite the emergence of this new paradigm, the previous paradigm based on mass production has continued to dominate – largely as a result of three factors. These include:

- International liberalisation that has opened up new markets;
- The development and spread of new flexible production systems, such as Toyota's just-in-time model that links production directly to customer orders and aims to eliminate waste and encourage continuous improvement;

- The suppression of wages. In OECD countries, the share of earnings in national income fell from 75% in the mid-1970s to 66% in 2005, with the decline being particularly severe in the US where the share of wages has fallen to its lowest level since 1929.[9]

The dotcom crash did not lead to a more generalised depression because losses were largely contained to on stock exchange (the NASDAQ), the recession was cut short by the drastic reduction in interest rates and the rapid rise in liquidity that followed the 9/11 attacks and because demand was sustained through new and expanding markets in the emerging economies, in particular China. However, these factors lay the ground for the housing bubble and the credit crisis of 2008/2009 which has in turn sown the seeds for the current sovereign debt crisis: downward pressure on wages created a problem of final demand, made worse in countries such as the UK and US, where there have been growing inequalities of pay among wage earners.[10] This was offset by a massive extension of credit to consumers as well as increased government spending - largely in the form of welfare payments and public sector jobs. At the same time, countries with large export surpluses and low levels of domestic demand (such as China) have provided credit to Western nations, especially the US.

What started as a 'credit crunch' in 2008 has turned into a sovereign debt crisis. Reductions in tax receipts, stimulus spending and growth in public spending have led to staggering debts and deficits. Herein lies the crux of the crisis: it has now become clear that governments too face budgetary constraints and it seems that they have now reached their borrowing limits. As Kenneth Rogoff argues, the global economy is over-leveraged and as such, the only solution lies in transferring wealth from creditors to debtors, either through inflation, defaults or financial repression.[11] This is why calling the current financial crisis the 'Great Recession' is fundamentally misleading. This crisis is not just a severe cyclical downturn – it is the result of longer-term structural weaknesses (namely the loss of dynamism of the old mass production paradigm) and as such, short-term monetary and fiscal measures to stimulate demand are unlikely to restore growth by themselves.

1.2. Understanding the new paradigm

Understanding the nature of the new paradigm is important for three reasons:

- First, these paradigm shifting technologies, namely new information and communication technologies will shape the nature and direction of innovation in the coming period. It is therefore important to identify these new 'innovation trends' and explore how and whether they are applicable to the social field.

[9] In the US the wage share of national income fell to 51% in 2006. By then the proportion of national income going to the top 10% of the population, which had been one third in the early 1970s had risen to nearly a half (48.5%). There was a parallel skewing of distribution of income in the UK, with almost all the gains from growth in recent years going to the top 10% of households, while half of all earners saw no growth in their incomes, and one third experienced a fall. As a result the measure of inequality (the Gini coefficient) which had risen sharply in the 1980s and again in the second half of the 1990s rose again as the bubble came to a head. See G Irvin, *Super Rich: The Rise of Inequality in Britain and the United States*, Polity Press, 2008; A Glyn, *Capitalism Unleashed: Finance, Globalisation and Welfare*, Oxford, 2006; G Irvin 'From Profit Squeeze to Wage Squeeze', *Renewal*, vol. 17:3, Autumn 2009; Congressional Budget Office, *Trends in the Distribution of Household Income Between 1979 and 2007*, Washington, Congressional Budget Office, 2011, viewed 21 May 2012, http://cbo.gov/publication/42729

[10] See 'Incomes are Stagnant' and 'Except Among Top Earners' in M Porter and J W Rivkin, 'The Looming Challenges to US competitiveness', *Harvard Business Review*, Vol. 90:3, March 2012

[11] See K Rogoff, 'The Second Great Contraction', *Project Syndicate*, 2nd August 2011, viewed on 19 April 2012, http://www.project-syndicate.org/commentary/the-second-great-contraction

- Second, there is an important relationship between paradigm shifting technologies and values and attitudes: the latter influences and shapes the former and vice versa. For example, the affluence and stability created during the 20th century (as a result of the mass production paradigm) led to a significant shift in values and attitudes among populations in Europe and North America. These 'new' values and desires for, among other things, autonomy and a better quality of life, have led to new patterns of consumption which are in turn driving innovation and social innovation. Values emerging from the new paradigm will drive innovation in the future. For now, however, there is a mismatch between contemporary values and the organisations with which individuals interact. This is a significant opportunity for social innovation.
- Third, there is a strong link between the social and environmental challenges we face and the mass production paradigm. Many of the social and environmental challenges we face, such as climate change and ageing, could be interpreted as a result of the 'success' of the mass production paradigm. In other cases, the institutions and structures that were established during the mass production paradigm are ill suited to dealing with 21st century challenges. For example, welfare states, which were based on mass production principles such as universal access to public services, standardised packages of care, centralisation, command and control styles of management, are poorly suited to dealing with diversity of need and complexity.

1.2.1. Innovation trends

These paradigm shifting technologies (ICT) will shape the nature and direction of social innovation in the coming period – by providing new tools, objectives and opportunities for social innovation. This may seem self-evident but it is important to mention how this is the case, not only to identify potential spaces for social innovation but also to understand how the field of social innovation might unfold and develop.

Perez has identified four emerging trends which are relevant to our inquiry. These are: the emergence of networks as the key organizational structure of the new paradigm; hyper-segmentation of markets or what is often called 'mass customization'; the hyper-segmentation of units of production and the emergence of small knowledge intensive enterprises (SKIEs) and; energy and the environment as a particularly important source of new innovations.[12] We believe that social challenges will be an equally important source of new innovations and this is borne out by recent research exploring the 'new nature of innovation.'[13]

These trends are inter-linked and mutually reinforcing. For example, the internet has enabled the hyper-segmentation of markets, which in turn has made it possible and profitable for small firms to cater to niche markets. At the same time, global firms have started to focus on their core competences and outsource their complementary activities. This is not about separating out innovative from non-innovative activities. Rather, it is about assessing which organisations are best placed to create value across different parts of the value chain. In this sense, industrial processes are being distributed in an attempt to gain creativity and flexibility. The Economist refers to this as the 'Third Industrial Revolution'.[14] In a recent report they reveal how the digitisation of production processes and the development of 3D printing is revolutionising manufacturing, "the factory of the

[12] Adapted from C Perez, *The financial crisis and the future of innovation: A view of technical change with the aid of history,* Working Papers in Technology Governance and Economic Dynamics no. 28, 2010.
[13] FORA, 'The New Nature of Innovation', Copenhagen, 2009, viewed on 21 May 2012
[14] 'The Third Industrial Revolution', Leader, *The Economist*, 21st April 2012

future will focus on mass customisation—and may look more like those weavers' cottages than Ford's assembly line."

Today, we see these trends (the emergence of networks, the hyper-segmentation of markets and units of production and so on) in the social field. It is our hypothesis that awareness of the differentiation of needs has led to moves in favour of personalisation and co-production; this in turn has put pressure on traditional public service delivery models and, together with cost pressures, encouraged the growth of small, flexible[15], smart[16] and specialised organisations which focus on social goals and meeting social needs. Moreover, we argue that the recent resurgence of the co-operative movement is another example of the move away from large centralised organisations in favour of decentralised forms of production and distributed networks.

Indeed, it is our contention that co-operatives are particularly well suited to the new paradigm and could be a significant source of social innovation. In the 20th Century, co-operatives were marginalised in centralised economies as a result of the rise of welfare states on the one hand and the rise of large multi-national corporations on the other. However, one of the features of the new paradigm is a return to the micro and decentralised forms of production. Co-operatives are a well established model for distributed forms of production. Second, the co-operative movement has already developed an infrastructure for supporting individual co-operatives, although this is more advanced in some countries than others. The co-operative movements in Italy and Spain, for example, have a particularly well developed co-operative architecture, linking co-operatives through federations, institutions and consortia at the industry or sectoral level and then geographically at the regional and national levels. Many of these institutions provide training and education, financial and back office support and other services which would be un-economical for individual co-operatives to develop in-house. In this way, individual co-ops have the benefits of scale, but retain the flexibility that comes with being a small firm. This is why the co-operative sector is so resilient. Third, co-operatives successfully marry social and economic goals.[17] In particular, co-operatives have democratic governance structures and experience of making them work effectively. This could be particularly relevant in the non-profit sector where one of the main criticisms is that charities tend not to include their beneficiaries in decision making processes; in the private sector as a means of creating trust and value for consumers, local communities and employees; and in the public sector as an alternative to privatisation or where citizens are being involved in the design and delivery of public services.

We need a better understanding of these trends and how they relate to social innovation. We will explore these issues in greater depth over the course of the TEPSIE project. We also need a better understanding of the relationship between new technologies, new needs and patterns of consumption and new organisational forms. This is what we turn to next.

1.2.2. Changing values and new needs

The affluence and stability created in North America and parts of Europe in the 20th Century, as a result of the mass production paradigm and cheap oil, led to a significant change in values and beliefs. This shift towards individualism and postmodern values is well documented in the

[15] M Piore and C Sabel, 'The End of Mass Production' in *Economy and Society*, vol. 16, Issue 3, 1987.
[16] WIRE 2011, Debrecen Declaration: Contributing to European competitiveness through integrated research and innovation policy - Clusters and research infrastructures working together. Available at http://www.wire2011.eu/upload/document/34/Debrecen%20Declaration.pdf
[17] Revised Rochdale Principles of Co-Operation, viewed on 21 May 2012, http://www.ica.coop/coop/principles.html

academic literature.[18] These values have led to changes in patterns of consumption, which in turn have shaped and driven innovation and social innovation.

Ronald Inglehart describes how "postmodern values bring declining confidence in religious, political, and even scientific authority; they also bring a growing mass desire for participation and self-expression…. today, the spiritual emphasis among mass publics is turning from security to significance: from a search for reassurance in the face of existential insecurity to a search for the significance of life."[19] In addition, he notes that "postmodernity values autonomy and diversity over authority, hierarchy and conformity." Zygmunt Bauman describes this change in values as a move from a 'solid modernity' which was characterised by security and stability (steady jobs, traditional family structures, the welfare state, fixed national identities and so on) to a 'liquid modernity' in which people abandon security and embrace freedom, together with the chaos and uncertainty that it entails.[20] James Maxmin and Shoshana Zuboff explain that, "the new individuals seek meaning, not just material security and comfort. They enjoy their things but place an even higher value on the quality of the lives they lead, in which those possessions play a part. They insist on self-expression, participation, and influence, because they share the certain knowledge that the singularity of their own lives cannot be deduced from the general case."[21] According to Maxmin and Zuboff, citizens 'yearn' for autonomy and 'psychological self-determination' and reject the 'mediated influence' of traditional institutions.[22]

Maxmin and Zuboff argue that institutions have failed to keep up with people's changing needs and desires, in particular, this rise in individualism and the "yearning for psychological self-determination." These new attitudes and beliefs are not reflected in contemporary organisations and the result is a chasm – or what they call the 'transaction crisis' between 'new individuals' and organisations which still operate under the enterprise logic of industrial age capitalism.

They claim that this chasm could sow the seeds for a new era of wealth creation and the next episode in capitalism – what they call the 'support economy'. This is because new needs and new patterns of consumption have historically played a critical role in changing the form and nature of organisations – namely, the practices, attitudes, and assumptions on which they are based: "epochal shifts in the logic of commerce – and of capitalism itself – have typically begun in response to underlying changes in the nature of society as they were expressed in new approaches to consumption. The record of the last quarter-century shows that business organisations do not easily change from within. Instead, the changes occurring outside the organisation – in the nature of consumption today – are most likely to be the source of the next fundamental transformation in the nature and purpose of business, as well as in the underlying logic of capitalism itself."[23]

In the social field, these changing values, together with the inadequacy of existing institutions, are the driving forces behind calls for 'direct democracy' and 'citizen engagement' and have led to a dramatic growth of social activism, especially grassroots activism, unconventional political activity,

[18] See for example, U Beck & E Beck-Gernsheim, *Individualization*, Sage Publications, London, 2001; P Norris and R Inglehart, *Sacred and Secular: Politics and Religion Worldwide*, Cambridge University Press, New York, 2004

[19] R Inglehart, *Modernization and Postmodernization: Cultural, Economic, and Political Change in 43 Societies,* Princeton University Press, 1997

[20] Z Bauman, *Liquid Modernity*, Polity Press, 2000

[21] J Maxmin & S Zuboff, *The Support Economy: why corporations are failing individuals and the next episode of capitalism*, Penguin Press, London, 2002

[22] J Maxmin & S Zuboff, *The Support Economy: why corporations are failing individuals and the next episode of capitalism*, Penguin Press, London, 2002

[23] J Maxmin & S Zuboff, *The Support Economy: why corporations are failing individuals and the next episode of capitalism*, Penguin Press, London, 2002

self-help groups, co-ops, and green and social movements.[24] These changing values are also at the root of recent trends towards pro-sumption and the recent explosion of social, political and organisational activity on the web.[25]

Clearly, values have shaped and influenced the form and nature of social innovation. We can also assume that new technologies will lead to new values (and vice versa). Therefore, understanding the interplay between new technologies, changing values, needs and patterns of consumption is critical to understanding new and emerging opportunities for social innovation.

1.2.3. Social and environmental challenges

There are a number of social and environmental challenges that have emerged as a result of the mass production paradigm. Our reliance on fossil fuels has had a significant role in driving climate change; the affluence and security created during the second half of the 20th century has led to significant demographic shifts; and contemporary lifestyles have led to new diseases, such as diabetes and obesity, and are placing new burdens on healthcare systems. Moreover, there is a growing mismatch the scale and nature of challenges and the institutions which are tasked with dealing with them. The most daunting challenges are climate change, ageing and chronic disease. These are a significant opportunity for social innovation.

In the case of chronic disease, for example, it is estimated that by 2020, these conditions will account for almost 60% of all diseases and roughly three-quarters of all deaths worldwide. At the moment, heart diseases are the most common form of chronic disease but obesity and diabetes are showing worrying trends – not only because they are affecting ever increasing numbers of people but also because they are starting to appear earlier in life. Obesity has already reached record levels – almost a third of all people living in Europe are overweight. Alarmingly, this trend is continuing at an increasing rate – especially among the young and poorer socio-economic groups.[26] There is a similar trend with diabetes – it is estimated that between 2010 and 2030, there will be a 69% increase in numbers of adults with diabetes in developing countries and a 20% increase in developed countries.[27] [28] As with climate change, pollution, criminal justice and poverty, the most effective policies are preventative, rather than curative, but these have been notoriously difficult to implement despite their apparent economic, health and social benefits.

There are then a range of issues resulting from demographic shifts. In Europe, people are living for longer and as a result, the population of working age is shrinking while the relative number of retirees is increasing.[29] The EU-27's old age dependency ratio is forecast to more than double from 25.9% in 2010 to 52.6% by 2060. Meanwhile, the total age dependency (which is the ratio of the total number of dependent people, both young and old compared with the total population aged

[24] J Maxmin & S Zuboff, *The Support Economy: why corporations are failing individuals and the next episode of capitalism*, Penguin Press, London, 2002

[25] R Murray, *Co-operation in the Age of Google*, Co-operatives UK, Manchester, 2010

[26] One study by the London Obesity Task Force found that 18% of children in Europe were overweight

[27] J E Shaw, R A Sicree & P Z Zimmet, 'Global estimates of the prevalence of diabetes for 2010 and 2030', *Diabetes research and clinical practice* Vol. 87. Pp. 4–14, 2010

[28] The prevalence of mental disorders and mental health problems is also on the rise. The condition expected to increase the most dramatically is dementia – from 7.7 million people in Europe in 2001 to 10.8 million in 2020. This is expected to double to 15.9 million by 2040

[29] The percentage of people over the age of 65 is set to rise from 17.4% in 2010 to 29.5% by 2060 and the proportion of those aged 80 years or above is forecast to triple during the same period. In 1960 there were on average three children (aged 0-14) for every elderly person (aged 65 and above), by 2060 there will be at least two elderly people for every child

15-64) is set to rise from 49.3% in 2010 to 77.9% in 2060. This inversion of the population pyramid will pose a radical challenge to two principal strands of 20th century welfare settlement – pensions and care for the elderly.

These trends are problematic for two reasons. First, there is a growing disconnect between traditional services and new needs – health services for example were originally designed to deal with acute rather than chronic disease, but it is chronic disease which is becoming more prevalent. Second, it has proved difficult to offset the growth in service need by equivalent reductions in cost. Schools, prisons, care homes and hospitals have cost structures with heavy overheads that are difficult to offset in labour intensive services.

The costs implications of an ageing population and the explosion of chronic disease are staggering. The European Commission predict that EU-27 Members will spend an additional 5% of GDP on pensions, health care, long term care, education and unemployment benefits up to 2060.[30] [31] [32] In the UK alone, the Office of Budget Responsibility predicts that age-related spending will exceed 27% of GDP by 2060, generating a public sector net debt of over 100%. Already, the demographic change in the UK is adding £1 billion a year to NHS costs. If radical policies cannot stem the increase in chronic disease, health services are forecast to grow to 14% of GDP in the EU by 2030. Figures are even more alarming for the UK and US, where public expenditure on healthcare is forecast to grow to 12% and 20% respectively by the early 2020s.[33] As a result, on current trajectories, the biggest sectors (both by value and employment) of Western economies in 2020 and beyond will not be cars, ships, steel, computer manufacturing or personal finance but rather health, education, and care.[34]

Similarly, the challenges posed by climate change will require profound changes, not only in terms of new technologies, but also in terms of individual behaviour. We will need to cut energy use, conserve what is used through recycling and re-use and avoid production where possible rather than expanding it. This requires innovation on a vast scale. Every part of the economy - from design and processing to distribution and consumption - will need to be transformed.

The devastating effects of climate change are now well documented – climate change is expected to lead to changes to agricultural production and threaten food security; lack of fresh water could lead to water insecurity (an extra 1.8 billion people could be living in water scarce environments by 2080); rising sea levels could yield a range of climate disasters; climate change is affecting ecosystems and biodiversity; it will require changes to infrastructure; and it will have significant effects on human health.[35]

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[30] European Commission (DG ECFIN) and Economic Policy Committee (AWG), 'Ageing Report: Economic and Budgetary Projections for the EU-27 Member States' (2008-2060), *European Economy* 2/2009

[31] This average does however, mark quite considerable variations across the member states. Nine member states (Luxembourg, Greece, Slovenia, Cyprus, Malta, Romania, Spain, the Netherlands and Ireland) are facing particularly significant increases in ageing related spending of 7% or more. See for example, European Commission (DG ECFIN) and Economic Policy Committee (AWG), Ageing Report: Economic and Budgetary Projections for the EU-27 Member States (2008-2060), European Economy 2/2009

[32] Long term care costs are also rising. In the UK, care is already approaching 4-5% of GDP. As a percentage of GDP, long-term care expenditure is expected to rise by 168% in Germany, 149% in Spain, 138% in Italy and 112% in the UK between 2000 and 2050

[33] A Wyke, *The Future of Healthcare in Europe*, Economists Intelligence Unit Limited, 2011

[34] R Murray, *Danger and Opportunity: Crisis and the New Social Economy*, NESTA, London, 2009

[35] See 'The Costs to Developing Countries of Adapting to Climate Change: New Methods and Estimates', *The Global Report of the Economics of Adaptation to Climate Change Study*, World Bank, Washington, 2010 and M Parry, N Arnell, P Berry, D Dodman, S Fankhauser, C Hope, S Kovats, R Nicholls, D Satterthwaite, R Tiffin & T Wheeler,

Similarly, there are significant financial implications to climate change and resource scarcity. The costs and impacts are hard to quantify and predict, but the broad consensus is that they will be considerable and wide-ranging. The Stern Review estimated that climate change would cost between 5% and 20% of global per-capita consumption, depending on how the costs are measured[36] and the World Bank has recently revised its estimates upwards and claims that the costs between 2010 and 2050 of adapting to a world which is 2°C warmer could amount to $75 billion to $100 billion a year for developing countries.[37] Nicholas Stern called for an investment of 1% of GDP to counter the dangers of a 20% reduction in global per capita growth as a result of climate change. The forecasted increases in health, education, pensions and care expenditures dwarf this figure, and threaten to swamp public budgets and in the case of pensions and health care, private budgets as well.

These social, environmental and demographic pressures are becoming ever more pressing at a time when public budgets are already squeezed. Social innovation is needed to address these challenges and to help modernise the institutions tasked with addressing them.

1.3. Conclusion

We are moving to a new paradigm, one that is based on information and communication technologies and characterised by networks, distributed and decentralised systems of production and the hyper-segmentation of markets. It is emerging as a result of new technologies, new needs and patterns of consumption and new organisational forms – each of which are overlapping, inter-linked and self-reinforcing.

The current crisis should be seen in this context; it is evidence of the weakening and exhaustion of the mass production paradigm. At the same time, the first green shoots of the new paradigm are emerging; organisations which are based on entirely new principles and assumptions. The emergence of the new paradigm is also creating and shaping new opportunities for social innovation. Indeed, many of the new trends in social innovation are either enabled by new technologies (mass collaboration, open innovation, pro-sumption, collaborative consumption and so on) or a direct response to traditional models which are in some way inadequate (for example, co-production, decentralisation and systems thinking).

However, even though this crisis marks one of the transition points to the new paradigm, it is not at all guaranteed that the potential of the new paradigm will be fully realised. Whether we enter a Golden Age or a Gilded Age depends on whether the powerful industries and organisations of the previous paradigm use the new technologies to strengthen their position, or whether new forces can re-shape the institutions and structures that will help spread the gains from the new technologies more widely. There is a significant role here for governments in making sure that the benefits of the new paradigm are widely distributed. We will explore the options and responses available to government in the next section.

Assessing the Costs of Adaptation to Climate Change: A Review of the UNFCCC and Other Recent Estimates, International Institute for Environment and Development and Grantham Institute for Climate Change, London, 2009

[36] N Stern, *The Economics of Climate Change: The Stern Review*, Cambridge University Press, Cambridge, 2007

[37] 'The Costs to Developing Countries of Adapting to Climate Change: New Methods and Estimates', *The Global Report of the Economics of Adaptation to Climate Change Study*, World Bank, Washington, 2010

2. Policy Responses to Support Social Innovation

Growing interest in social innovation to help address these societal changes has been reflected in government policy. Many governments are supporting the field through innovation funds, dedicated teams, investment tools, support for social enterprises, and so on. Some of these are intended to promote social innovation outside the public sector, most notably through capacity building support for the third sector and social enterprises. Other policies and initiatives aim to promote social innovation within the public sector, especially in the delivery of public services.

It is important to note the variety both in terms of the kinds of policies that have been implemented and the speed with which governments have taken up the social innovation agenda across Europe. This variety reflects the diversity of national contexts. The Nordic countries have been most open to social innovation as a means of renewing their social model and promoting their social and economic performance. The Anglo-Saxon countries have been quick to adopt the social innovation agenda, especially in terms of supporting social enterprise in order to diversify public service provision. In Continental and Mediterranean countries social innovation has been seen largely as an add-on and has often failed to penetrate traditional institutions. Across Eastern Europe, the lack of well-established civil societies has hindered the progress of social innovation. Instead, government policies have tended to focus on public service provision and developing the third sector.

In this section we provide a snapshot of policies to support social innovation. We have taken an international perspective in order to be able to include some of the leading examples of government policy to promote social innovation. We have identified the following policy areas and organised the material accordingly:

- Strategy
- Innovation units, agencies and institutions
- Finance
- Tax, laws and regulation
- Procurement and commissioning
- Metrics

2.1. Strategy

There are very few examples of explicit social innovation strategies. One notable example is in the Basque Country in Spain. This region was an early adopter of the term 'social innovation' through its inclusion in regional strategic plans. This was reinforced by the creation of a Strategic Plan for Social Innovation in February 2011. [38] The City of Bilbao has also made a commitment to social innovation through the creation of the DenokInn Social Innovation Park.

However, social innovation is being put on the agenda in other ways – either through initiatives to support aspects of social innovation (such as social enterprise or public sector innovation) or as part of a broadening of the concept of innovation to include social innovation as well as business and technological innovation.

[38] Viewed 21 May 2012, www.innobasque.com

Indeed, one recent trend, recommended at the European Level by the European Technology Platforms, the European Research Area and the Business Panel on Future EU Innovation Policy, has been to broaden the concept of innovation to include social innovation and to re-focus research and development around grand societal challenges. This has been taken up by the Swedish government which is currently developing a new national innovation strategy to improve the climate for innovation.[39] The strategy is planned to be in place in autumn 2012 led by the Ministry of Enterprise, Energy and Communications but involving all ministries. Clear efforts have been made to include social innovation in the strategy and give it significant weight. The importance of this has been stressed by Minister of Enterprise, Annie Lööf. Similarly, in Austria, the Strategy of the Federal Government for Research, Technology and Innovation, published in 2011, advocated taking a "broad approach to innovation that not only includes technological, research-driven and non-technological innovations in manufacturing and in the service sector but also ecological and social innovations as well as innovations in the public sector."[40] One of the key messages of this strategy is that social innovation is necessary, important and effective from a social as well as economic perspective and that social innovation is needed to tackle social and environmental challenges.

As part of its Europe 2020 Strategy launched in 2010, the European Union has launched the Innovation Union as one of its seven flagships.[41] This includes an "increasing social benefit" initiative and a European Social Innovation pilot and hub[42] designed to mainstream social innovation through the European Social Fund, as well as research programmes on public sector and social innovation.

Another trend has been the growing importance of public sector innovation. Increasingly, governments are making innovation in public services a priority. For example, Canberra launched an Australian Public Service (APS) Innovation Action Plan in 2011.[43] Ministers from across the service signed the plan as a demonstration of their commitment to fostering innovation in the Australian Public Service. The Action Plan provides the APS with a framework for embedding innovation in its work. Building on this, the Department of Industry, Innovation, Science, Research and Tertiary Education has created an online resource to help public servants develop and apply innovative solutions. The toolkit includes a diagnostic tool to assist in thinking about organisational strengths and weaknesses, guidance on how to integrate innovation into operations and a section on barriers to public sector innovation.[44]

2.2. Innovation units, agencies and institutions

Over the last decade, new teams, units and agencies have been set up within and outside the public sector with the explicit purpose of supporting innovation. This trend is based on the recognition that the competencies, mindsets and environments needed for innovation are not necessarily the same as those required for day-to-day operations and service delivery.

[39] Viewed 21 May 2012, http://www.regeringen.se/sb/d/14440
[40] *Becoming an Innovation Leader, Realising Potentials, Increasing Dynamics, Creating the Future*, Austrian Strategy of the Federal Government for Research, Technology and Innovation, Vienna 2011
[41] http://ec.europa.eu/europe2020/index_en.htm
[42] Social Innovation Europe: http://www.socialinnovationeurope.eu/
[43] Viewed 21 May 2012, http://www.innovation.gov.au/Innovation/PublicSectorInnovation/Pages/default.aspx
[44] Viewed 21 May 2012, http://innovation.govspace.gov.au/

2.2.1. Innovation units

There has also been a proliferation of innovation units and labs. Some innovation units are completely independent and operate outside government. One example is The Australian Centre for Social Innovation (TACSI), founded in 2009 with seed funding from the South Australian government. [45] TACSI funds and supports a variety of social ventures and social entrepreneurs across Australia through the Bold Ideas, Better Lives Challenge. It also houses a Radical Redesign team which co-designs and prototypes solutions to social challenges using a 'Working Backwards' approach. One example of their work is Family by Family, a new model of family-to-family support which was developed with 100 South Australian families. Another example is the New Zealand Centre for Social Innovation (NZCSI), which brings together the public, non-profit and business sectors to create solutions to New Zealand's most pressing social challenges. Its most recent initiative is the creation of the Social Entrepreneurs School which will support 15 early stage social entrepreneurs to build sustainable social ventures.

Other innovation units begin as part of the public sector and are later spun out to become independent. One example is the Innovation Unit in the UK that originated in the Department of Education and is now an independent innovation intermediary for public services. It has focused on supporting innovation in schools and children's services, the third sector, and local government.[46]

Some innovation units work within local government – such as SILK (the Social Innovation Lab Kent) in the UK. SILK was set up in 2007 by Kent County Council as a hub for social innovation within the local authority. It was established to provide a creative environment for a wide range of staff to work together on some of the biggest challenges facing the local authority. It was also set up to test new approaches to user-centred innovation. SILK has done this by linking the internal operations of the local authority with inputs from citizens and other innovators.[47] Other innovation units support local governments. One such example is the 27e Region, an innovation unit based in Paris, established in 2008, and supported by the Association des Régions de France, the Caisse des Dépôts and the European Commission.[48] It acts as a laboratory for the 26 French Regional Councils with the purpose of fostering creativity, innovation and sustainability in public institutions through community projects, prototyping and design thinking. The idea is to facilitate collaboration that enables localities to innovate together by sharing knowledge and risks.

Some innovation units work within and across government departments. The most notable example of this is MindLab in Denmark. MindLab is a cross-departmental innovation unit that involves citizens and businesses in developing solutions for the public sector.[49] Another example is the Helsinki Design Lab (HDL), which is Sitra's internal design team.[50] Like MindLab and SILK, HDL uses design thinking as a means of generating social innovations. Unlike the other two, which develop incremental innovations, HDL aims to use Strategic Design as a way of re-thinking and re-designing whole systems. Its activities include hosting a platform to share work and case studies, running a symposium event (HDL Global) and convening strategic designers and content experts in studio sessions (HDL Studios).

[45] Viewed 21 May 2012, http://www.tacsi.org.au/
[46] Viewed 21 May 2012, http://www.innovationunit.org/
[47] Viewed 21 May 2012, http://socialinnovation.typepad.com/silk/
[48] Viewed 21 May 2012, http://www.la27eregion.fr/
[49] Viewed 21 May 2012, http://www.mind-lab.dk/en
[50] Viewed 21 May 2012, http://helsinkidesignlab.org/

2.2.2. Innovation offices and departments

New government departments supporting social innovation, the third sector and social enterprise are also appearing. Examples include the Office for Civil Society in the UK (previously the Office of the Third Sector) and the Office of Social Innovation and Civic Participation in the USA.[51]

The Office of Social Innovation and Civic Participation (OSICP) was set up by the Obama Administration in 2009 to uncover and support community solutions to major societal challenges. The Administration's Community Solutions Agenda is based on three main goals: to promote service as a solution and a way to develop community leaders; increase investment for innovative solutions that demonstrate results; and develop new models of partnership. Particular initiatives include the establishment of the Social Innovation Fund at the Corporation for National and Community Service, the Invest in Education Fund at the Department of Education, programmes to promote national and community service opportunities, such as United We Serve, the establishment of a range of prizes and challenges as well as initiatives to create better mechanisms to measure and evaluate projects and programmes. Some were sceptical that government would be a good partner in finding and investing in innovation but after three years, there are some encouraging signs that the OSICP has helped create an environment that is conducive to greater innovation.[52]

In the UK, the Office of Civil Society (OCS), which sits within the Cabinet Office, has specific responsibility for leading and implementing practical policies and initiatives relating to the government's flagship 'Big Society' agenda. Even though the OCS is not tasked specifically with supporting social innovation, many of the programmes and initiatives it is developing will support aspects of social innovation. The OCS works across 5 main areas: Big Society policy and analysis; public services; charities and sector support; social investment and social enterprise; and social action. The aim of this government office is to 'deliver radical change in the relationship between citizen and state' and in particular to: make it easier to run a charity, social enterprise or voluntary organisation; get more resources into the sector and strengthen its independence and resilience; and make it easier for sector organisations to work with the state.

The OCS has overseen and developed a range of initiatives and programmes – Big Society Capital, the Innovation in Giving Fund, Social Impact Bonds (see below) as well as the Mutuals Pathfinder Programme which involves spinning out public services into employee-led mutuals and co-operatives. My Civil Service Pension (MyCSP) was the first to be launched as a mutual venture in 2011 under this programme.

2.2.3. Innovation agencies

Recently, governments in the UK and US have focused innovation policy on creating the conditions for innovation – namely, supporting a strong skills base, the establishment of innovation clusters and creating the right fiscal and regulatory conditions for innovation, together with strong legal protection for new innovations. However, this 'minimalist view' of government innovation policy has been criticised. In her recent publication, *The Entrepreneurial State*, Mariana Mazzucato reviews the evidence and shows that targeted government spending on the 'most uncertain' phase of research and development can be an effective and successful way of promoting innovation and economic growth.[53] Indeed, research has shown that direct funding for early stage research in

[51] Viewed 21 May 2012, http://www.cabinetoffice.gov.uk/resource-library/office-civil-society-structure-finalised
[52] M Jolin, 'Social Innovation in Washington, D.C.', *Stanford Social Innovation Review*, Summer 2011
[53] M Mazzucato, *The Entrepreneurial State*, Demos, London, 2011

potential growth areas, which is often too risky for private investment, has yielded some of the most significant innovations over the last few decades. Indeed, there is a critical role to be played by government in this respect. This is well recognised by the most effective innovation agencies – examples include Tekes in Finland and Vinnova in Sweden.

Increasingly these innovation agencies are taking a broader view of innovation – to include service based, design related and social innovations as well – and are focusing their activities around social and environmental challenges. Vinnova, for example, Sweden's innovation agency, introduced a new strategy in 2010 to refocus its activities around global challenges facing Swedish industry and society. These four social challenges are health, wellbeing and medical care, competitive industry, sustainable and attractive cities, and information society 3.0. Vinnova was set up in 2001 to promote sustainable growth in Sweden by funding needs-driven research and the development of effective innovation systems. It does this by investing in research and development, capacity building for SMEs, forging global links, policy development and developing the innovation infrastructure in Sweden. Vinnova invests 220 million Euros in new and ongoing projects every year. Similarly, Tekes, the Finnish innovation agency, launched a new strategy in 2011 which highlights the importance of non-technical innovations – in particular social innovation – and has focused its activities to include social and environmental challenges. The strategy includes 6 focus areas: natural resources and sustainable economy (including renewable energy); vitality of people (health, care and learning); intelligent environments; business in global value networks; value creation based on service solutions and intangible assets and; renewing services and production by digital means. [54] According to a recent evaluation of its impact and activities, Tekes funded more than 60% of well-known Finnish innovations between 1985 and 2007 and in 80% of these cases, the funding had a significant impact. In addition, for every 13,000 Euros of Tekes funding, one permanent job is created in the private sector and in the funding of SMEs, every Euro invested by Tekes yields approximately 21 Euros of turnover annually. This suggests the important role to be played by innovation agencies in supporting social innovation.

2.3. Finance

There are many ways of organising public sector budgets to promote innovation. Departmental budgets can be top sliced for innovation, for example, 1% of turnover as a rough benchmark. Cross-cutting budgets can be used to support broad programmes which leave space for experimentation, such as the UK 'Invest to Save' budget. Outcome-based budgets can give greater freedom to providers to determine how they achieve outcomes, such as lower unemployment. Various devices have been developed to improve the financial incentives for innovation, especially ones that deliver gains to other public agencies although these are easier to design for products than services. The financial gains from innovation can be ring-fenced for initiators and developers. Or innovation-related pay can be introduced through institutional, team and personal performance bonuses linked to innovation. However these have proven hard to operationalize in many cases, and like many bonus structures can be divisive and problematic. The most interesting developments have been specific funds for social innovation and social enterprise and new financial instruments to support and promote social innovation.

[54] *Tekes Strategy: growth and wellbeing from renewal*, Tekes, Helsinki, 2011, viewed 21 May 2012, www.tekes.fi/en/Strategy

2.3.1. Innovation funds

One of the most important sources of finance for social innovation has often been dedicated public funds for early stage ideas, investment, R&D, and incubation. In 2010, the Government of Western Australia launched a Social Innovation Grants Program to promote innovation in the delivery of social and community services. Funding of A$2 million was made available in 2010-11 and $4 million thereafter for each year of the program.[55]

Another example is the Social Innovation Fund (SIF) run by the Office of Social Innovation and Civic Participation in the US.[56] The SIF awards grants ranging from $1-5 million to grant making intermediaries which then match the federal funds and hold competitions to identify the most promising non-profit organizations. Once selected, these non-profits must also match the funds they receive, and participate in rigorous evaluations of their programmes. One of the common criticisms is that the Social Innovation Fund explicitly limits its scope to social entrepreneurs and non-profit, community based organizations, which restricts the sources and kinds of innovative solutions the fund can support.

Other examples in Europe include Sitra in Finland, Argengufond in Estonia and Futurebuilders and the Social Enterprise Investment Fund in the UK. Sitra is an independent fund that reports directly to the Finnish Parliament. Originally its main focus was venture capital investments in technology-based enterprises but its remit was broadened in 2004, to anticipate the impact of social change in Finland and promote sustainable growth. Sitra's core activities are fixed-term research programmes centred on the following themes: sustainable lifestyles and smart use of natural resources, renewable leadership and well-being services, and bottlenecks of economic growth. These operations are funded from the returns of Sitra's endowment capital and investments.[57]

Inspired by Sitra, the Estonian Development Fund (Argengufond) was launched in 2007 to initiate and support changes in the Estonian economy and society. This is achieved through foresight projects, venture capital investments and innovation labs which provide a space for dialogue about new ideas, initiatives, and potential methods of implementation. The current projects are working towards policy reform in line with Estonia's developmental vision based on innovative thinking.[58]

Another example is the Futurebuilders Fund which is managed by the UK's largest social investor, the Social Investment Business.[59] Its role is to invest in third sector organisations delivering public service contracts to improve their financial and strategic capability.[60] A recent evaluation showed that Futurebuilders had been fairly successful in building the capacity of the third sector to deliver public services.[61] Social Investment Business also runs the Social Enterprise Investment Fund in the UK. This was launched in 2007 by the Department of Health with around £100m to prompt innovation in health and social care.

In the UK, the most significant development in this space is Big Society Capital (BSC), the first social investment market builder. BSC was launched in 2012 as an independently run social investment fund that aims to create a market for social finance which will deliver a mixture of social and

[55] Viewed on 21 May 2012, http://www.communities.wa.gov.au/grantsandfunding/Grants/SocialInnovation/
[56] Viewed on 21 May 2012, http://www.whitehouse.gov/administration/eop/sicp/initiatives/social-innovation-fund
[57] Viewed on 21 May 2012, http://www.sitra.fi/en
[58] Viewed on 21 May 2012, http://www.arengufond.ee/eng
[59] Viewed on 21 May 2012, http://www.futurebuilders-england.org.uk/
[60] Viewed on 21 May 2012, http://www.futurebuilders-england.org.uk/
[61] P Wells, T Chadwick-Coule, C Dayson, G Morgan, *Futurebuilders Evaluation: Final report*, Centre for Regional Economic and Social Research, Sheffield Hallam University, 2010

financial returns. BSC will eventually be capitalised with around £600m, two-thirds of which will come from dormant bank accounts and the rest from Barclays, HSBC, Lloyds Banking Group and the Royal Bank of Scotland. It is also seeking to encourage diversified sources of capital in the market. Investment will be delivered through social investment finance intermediaries (SIFIs) to social sector organisations (charities, social enterprises, voluntary and community organisations, cooperatives and mutuals). The belief is that by supporting SIFIs to grow and become more sustainable, they will be able to bring millions more in investment into the social sector than BSC itself. But it is equally important that social sector organisations are investment ready so that they can benefit from this income stream. [62]

2.3.2. Financial instruments

There are also a series of financing instruments which aim to capture social value and provide better incentives for public organisations to make preventative investments. Investing in social innovation is often complicated by problems associated with quantifying the effects of an investment, especially where those effects are not financial.

One of the most significant developments in the last few years is the creation of Social Impact Bonds (SIB). These are a financial tool being developed in the UK and elsewhere to provide a new way to invest money in social outcomes. They are a form of outcomes-based contracts in which the public sector agrees to pay for significant improvements in social outcomes (such as a reduction in re-offending, or in the number of people being admitted to hospital) for a selected group. This prospective income can then be used to raise capital from commercial, public or social investors which is used to pay for interventions, which are delivered by service providers with a proven track record. Financial returns to investors are made by the public sector on the basis of improved outcomes and if they do not improve, then investors do not recover their investment. In such a way, SIBs provide up front funding for prevention and early intervention services whilst removing the risk that interventions do not deliver outcomes from the public sector. This is possible where outcomes are measurable and lead to tangible public financial savings.[63]

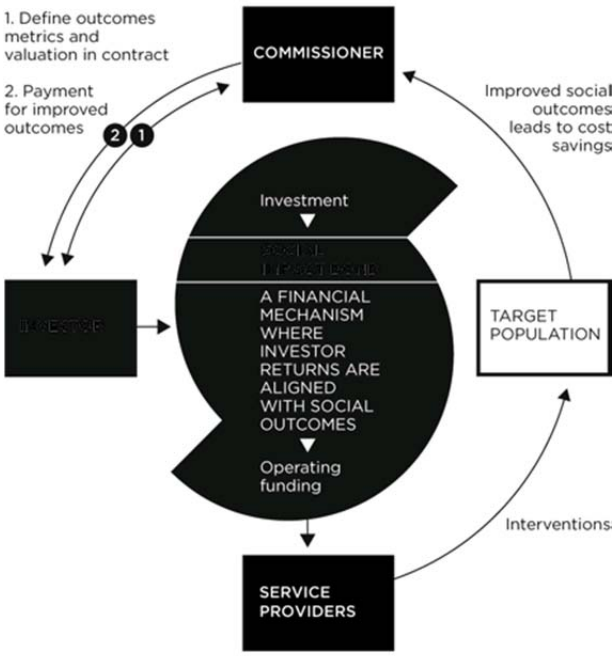
There is a range of models and variations being explored at local and national government level. The first Social Impact Bond in the UK was launched by Social Finance in September 2010. The six-year SIB pilot scheme in Kalyx-run Peterborough prison is to prepare around 3,000 short term prisoners for their lives post-release. If re-offending drops by more than 7.5% within six years, investors will receive a payment representing a proportion of the cost of re-offending. In November 2011 Social Finance published a progress report. After one year the proportion of individuals using the service was relatively high but levels of re-offending were difficult to gauge and it was not clear whether reoffending was reduced enough to generate a return to investors.[64]

In the US, Social Impact Bonds have been called Pay for Success Bonds. A report from the Center for American Progress released in February 2011 analysed their potential.[65] Local government officials in Massachusetts, New York City, and elsewhere are now investigating how SIBs could be applied in the areas of homelessness and criminal justice. Interest in SIBs has been boosted by the Obama Administration's focus on pay-for-success programs and its 2012 announcement that two agencies would use competitions to support pay-for-success pilots. But with only one example of a

[62] Viewed on 21 May 2012, http://www.bigsocietycapital.com/
[63] Viewed on 21 May 2012, http://www.socialfinance.org.uk/work/sibs
[64] Social Finance, *Social Impact Bonds: The One Service. One Year On,* 2011
[65] J B Liebman, *Social Impact Bonds: A promising new financing model to accelerate social innovation and improve government performance*, Centre for American Progress, 2011

SIB to date, and no track record as yet, a number of questions remain open: where SIBs could be most useful, how they should be structured, and whether they will actually work. In the near term, SIB investors are likely to be charitable foundations or philanthropists who prioritize societal benefit over financial rewards.

Figure 2: Structure of a social impact bond



Source: http://www.socialfinance.org.uk/work/sibs

2.4. Tax, laws and regulation

The state is also responsible for shaping the conditions in which innovators operate – traditionally, this is achieved through taxation, legislation, regulation and property rights. Despite recent research which shows that 'creating the conditions' for innovation is insufficient to promote innovation-led economic growth[66], and that supply side measures including direct investment are also critical, regulation, legislation and fiscal incentives remain an important plank of innovation policy.

2.4.1. Fiscal incentives

Fiscal incentives for social innovation can take the form of tax relief as in the case of the UK's Enterprise Investment Scheme (EIS) for social enterprises, or property tax holidays for early-stage social enterprise and charities. Tax incentives can be used to encourage businesses that meet higher standards of social and environmental performance. This can include providing lower corporate tax rates for businesses and/or lower capital gains tax rates for investors. R&D tax credits give tax relief for organisations to raise their investment in R&D for the design and development of innovations. Tax credits usually work by allowing organisations to deduct qualifying expenditure on R&D activities when calculating their profit for tax purposes.

[66] M Mazzucato, *The Entrepreneurial State*, Demos, London, 2011

In Austria, tax privileges are available for non-profit organisations with a "public utility" in the fields such as healthcare, child and family welfare, elderly care and vocational training etc. In Germany, similar activities carried out by social enterprises are granted tax exemption.[67] Whilst in Slovakia there is an income tax policy which stipulates that every person and company can declare assignation of 2% of their paid taxes to specific non-profit organisations listed in official registers.

Tax incentives can also be applied geographically as with experimental zones. These are used as a test bed for new ideas that can then be rolled out on a larger scale. In the 1990s in the UK, Employment Zones allowed contractors to innovate new methods for getting unemployed people into work, with payment linked to outcomes. Another example of a fiscal incentive is feed-in tariffs such as those used to accelerate investment in renewable energy technologies. They do this by offering long-term contracts to renewable energy producers. Renewable electricity generators are paid a cost-based price for the electricity they produce. The tariff may differ to enable various technologies to be profitably developed.

2.4.2. Regulation

Regulation can encourage behaviour change and in so doing support social innovation. In principle, this can be applied to all policy areas but the current focus is predominantly around environmental regulation. For instance, congestion charging in major cities is encouraging consumers to switch from motor vehicles to more environmentally sustainable forms of transport and encouraging suppliers to respond to their demand, with new hybrid cars. In Germany, the government has used regulation to develop renewable-energy solutions.

2.4.3. New legal forms

Another development over the last decade has been the creation of new legal forms for social businesses. These new legal forms have helped to build awareness of the social enterprise sector and distinguish social enterprises from charities, associations and other mission driven organisations. In general, these legal forms prevent the full distribution of profits. One example is the Community Interest Company (CIC) in the UK. Companies that register as a CIC retain their traditional form (as co-ops, or companies limited by guarantees or ordinary limited companies). They have an "asset lock" to prevent the assets and profits being distributed and they have to file a report every year to demonstrate their impact on the relevant community of interest. Another example is the 'Social Purpose Company' created in Belgium in 1995. This status explicitly stipulates that the organisation's mission is to create social profit and not the accumulation of wealth by its associates. Since its launch, take-up of this legal status has been very low (about 450 existed by 2008). This is arguably due to the balance between the tax advantages it offers and the reporting constraints. Other examples include the French "Collective Interest Cooperative Society", the Portuguese "Social Solidarity Co-operative" and the Spanish "Social Initiative Co-operative".

2.4.4. New rights

Extending the rights of individuals and communities or giving them new rights is another lever to promote social innovation. In some countries, opt out rights have been created for communities to design and run their own services in place of existing state, regional or national bureaucracies.

[67] Austrian Institute for SME Research, *Study on Practices and Policies in the Social Enterprise Sector in Europe,* viewed 21 May 2012, http://ec.europa.eu/enterprise/newsroom/cf/_getdocument.cfm?doc_id=3408

One example is the Localism Act, introduced in the UK in 2011, which gives local communities two new rights. The first, the Community Right to Buy, allows important local amenities and buildings - such as community halls, shops or pubs to be nominated for listing by the local authority as assets of community value. If these assets come up for sale, communities will be given additional time to prepare a bid to take them over, making it easier to keep highly priced assets in public use and part of local life. Sharing public assets with civil society is a way of getting more value from them and supporting community engagement at the same time. The second, the Community Right to Challenge will allow voluntary and community groups, parish councils and local authority staff to take over the running of local public services. The aim is to enable local citizens to play a bigger role in designing and delivering local services. This could be very wide ranging, including managing a park, running a transport service, or providing social care. The government has also announced that community groups will be supported to use the Community Right to Challenge through a delivery body.[68]

2.5. Procurement and commissioning

Through procurement and commissioning, governments can support the development of social innovations, accelerate the widespread adoption of social innovations and stimulate the creation of new markets. A study for the European Commission on innovation and public procurement highlights the growing support and need for the use of public demand to stimulate innovation and the creation of new markets.[69] Public procurement can support social innovation at every phase of the innovation lifecycle: in the initiation phase (where no established market exists for a particular good or service); in the escalation phase (by acting as an early adopter of a good or service and demonstrating its value to the wider market) and; in the consolidation phase (governments can create 'critical mass' for the adoption of a new good or service).[70]

In reality, however, existing commissioning and procurement structures tend to be poorly designed for social innovation. In many cases, contracts are too short-term, place excessive risk on providers, set unrealistic prices which prevent full cost recovery, and involve an excessive burden of monitoring and evaluation. As such, procurement structures and processes tend to favour larger, more established providers, rather than new, more innovative organisations. These factors make it difficult for social enterprises and third sector organisations to access capital and take up opportunities to deliver services. Reforms which encourage contestability and diversity of providers can help to promote innovation.

Public procurement systems vary significantly between countries. Some countries have a highly centralised system with clear guidelines as in the case of Denmark while others have a decentralized system such as the Netherlands. In a few countries explicit efforts are being made to incorporate social innovation into procurement. In recent years, the Finnish government has been promoting environmental sustainability through reforms to public procurement.[71] In Denmark, organisations such as National Procurement Inc, which is jointly owned by national and regional public agencies, have used their purchasing power to stimulate environmentally friendly innovations. And in Italy, a law was passed in 1991 to reserve certain public contracts to social co-

[68] Viewed on 21 May 2012, http://www.communities.gov.uk/localgovernment/decentralisation/localismbill/
[69] J Edler et al., *Innovation and Public Procurement: Review of Issues at Stake, Study for the European Commission-Final report*, Fraunhofer Institute for Systems and Innovation Research, 2005
[70] J Edler et al., *Innovation and Public Procurement: Review of Issues at Stake, Study for the European Commission-Final report*, Fraunhofer Institute for Systems and Innovation Research, 2005
[71] Viewed on 21 May 2012, www.tem.fi

operatives.[72] Recent developments include outcomes-based commissioning, practice based commissioning and social clauses in contracts.

2.5.1. Practice-based commissioning

Practice-based commissioning involves devolving commissioning powers to front line practitioners. This can provide the space and freedom to experiment and remove the cost and control of unnecessary bureaucracy. Practice-based commissioning (PBC) has played a major role in health reform in England. It has involved providing front line clinicians with the resources and support to become more involved in commissioning decisions based on the principle that they are in a prime position to translate patient needs into redesigned services. Questions have been raised about the extent to which PBC has been successfully implemented and whether it is achieving its objectives. In 2008 the NHS Next Stage Review acknowledged that PBC had not lived up to its potential, and set out the government's vision for redefining and reinvigorating PBC.[73]

2.5.2. Outcomes based commissioning

Outcomes based commissioning is where a commissioning body agrees to fund a provider on the basis that they will achieve particular agreed outcomes (rather than deliver particular outputs). The provider does not have to specify how they will achieve these outcomes. One of the problems with existing procurement structures is that they tend to freeze innovation over the course of the contract. Outcomes based commissioning aims to overcome this by enabling providers to innovate during and over the course of the programme. It is therefore hoped that outcomes based commissioning will help to create services which are tailored to the needs of service users. In the UK, this has prompted a series of developments including Local Area Agreements and Comprehensive Area Assessments, which seek to base local service commissioning, delivery and evaluation on an agreed set of outcomes for that area rather than on central targets. Other examples include Social Impact Bonds and Payment by Results.

2.5.3. Social value clauses

There is also growing interest in including social value or community benefit clauses into procurement contracts. These could include, for example, a requirement for the integration of disadvantaged workers or a requirement to make services available for specific target groups or communities. However, the practice of inserting social criteria into public contracts is not yet very common in the European Union. Proposals for social value clauses in England and Wales have been put forward in the Public Services (Social Value) Bill, which is currently making its way through the House of Lords. Under the Bill, all public bodies in the UK will be required to consider economic, social and environmental wellbeing when a service is being commissioned.

2.6. Metrics

Metrics are important for three reasons: they help to build a knowledge base by assessing and evaluating what works; they guide investment decisions; and shape public policy. Reliable metrics for social innovation are therefore critical in developing the field. They are important at the programme or project level to identify what works and what does not. This information can then

[72] J Defourny & M Nyssens, 'Social Enterprise in Europe : Recent Trends and Developments', *Social Enterprise Journal*, Vol. 4:3, pp. 202-228, 2008

[73] Viewed on 21 May 2012, http://www.dh.gov.uk/en/Publicationsandstatistics/Publications/PublicationsPolicyAndGuidance/DH_085937

be used to share and spread learning across the field as well as guide philanthropic and public investment decisions. Effective metrics about the scale, scope and impact of social innovation at the regional and national level would help guide policy makers in developing the right framework conditions for social innovation.

At the project level, there is now a range of metrics which capture social and environmental impacts as well as traditional economic measures. There is also a range of methods for measuring social impact and social value. Other metrics combine qualitative as well as quantitative data. The most notable examples include Social Impact Assessment, Environmental Impact Assessment, Social Return on Investment, 'Blended Value' and Triple Bottom Lines.[74] Some of these tools have been used by public bodies. EQUAL's use of SROI, for example, showed interesting outcomes in Austria, where the Chance B Hausmeisters project was found to generate a public profit of nearly €200,000.[75]

At the organisational level, there are a range of social accounting methods which measure the social and environmental effects of an organization's activities on particular social groups and on society at large. France's Bilan Sociétal (literally – social balance sheet) is a set of indicators showing how enterprises affect society. In Italy, the Bilancio Sociale[76] is a similar tool which can be used to raise levels of transparency. For example in the Agenzia di Cittadinanza project in Milan, the technique is used to take indirect benefits into account such as the added income generated by the provision of childcare that allows more parents to go out to work. From 2007 it became mandatory for all registered social enterprises.[77]

Measuring social innovation at the national and regional level, however, is fraught with difficulties. Traditional innovation metrics, which have been criticised for failing to keep pace with the changing nature of innovation, have limited use for the field of social innovation. Despite this, some governments have sought to measure the level of innovation within the public sector and other governments around the world are developing broader measures of growth and prosperity that take into account wellbeing and social and environmental factors.

2.6.1. National social innovation metrics

Traditional innovation metrics, which focus on inputs and outputs, are largely unhelpful to the field of social innovation, where outcomes and processes are more important and need to be assessed. Increasingly, traditional innovation metrics have been criticised for failing to capture the new and changing nature of innovation. Existing metrics were designed for a manufacturing based linear model of innovation, based on research and development and the creation of new scientific knowledge. This is why innovation metrics today include R&D expenditure, patent production and numbers of science and technology graduates. However, these metrics fail to capture innovations in services, in the public sector, the creative industries or new trends in user-led and open innovation. Policy makers around the world are demanding new innovation metrics to take into

[74] See for example, C J Barrow, *Social Impact Assessment: an Introduction*, Arnold, London, 2000; H A Becker, *Social impact assessment: method and experience in Europe, North America and the developing world*, UCL Press, London, 1997; N Scholten & G Olsen, *SROI A Guide to Social Return on Investment*, Lenthe Publishers, 2006

[75] Equal opportunities for all - Delivering the Lisbon Strategy through social innovation and transnational cooperation , 16/02/2009, viewed on 21 May 2012, http://ec.europa.eu/employment_social/equal_consolidated/data/document/Equal%20opportunities%20for%20all.pdf

[76] Viewed on 21 May 2012, www.bilanciosociale.it

[77] Viewed on 21 May 2012, www.impresasociale.net/

account this changing nature of innovation.[78] New ways of measuring the outcomes of innovation or value derived from new innovation processes would have significant relevance to the field of social innovation.

The EU's Social Innovation Europe initiative recently undertook a study of possible models and methods of measuring social innovation at the national and regional level which they will report on in 2012.[79] They advocate moving towards a Social Innovation Scoreboard, testing a suitable social innovation indicator within the Community Innovation Survey, and prototyping a rapid assessment tool for regions and cities on support for social innovation in their area.

2.6.2. Public sector innovation metrics

Some governments have sought to gauge the level of innovation in the public sector. The Government Innovation Index (GII) developed by the Government of South Korea looks at various areas to determine how well an organization innovates within changing environments. The index helps to diagnose levels of innovation, identify weak areas, and develop action plans to improve innovation capacity. The overall results of the index can serve as a reference for national innovation strategies. Similarly, the Australian Public Sector Innovation Indicators Project seeks to improve the measurement of public sector innovation in Australia. The aim of the project is to measure and evaluate the public sector's innovation performance and to benchmark this against other OECD countries. As part of the project the team have developed a new data collection tool - the Australian Public Sector Innovation Survey - and a new measurement tool - the Australian Public Sector Innovation Indicators. This project is still in its development phase. However, by the end of 2012, it is envisaged that they will have conducted a pilot public sector innovation survey, published initial findings as well as a paper detailing their measurement framework.

The OECD is currently setting up an Observatory of Public Sector innovation to be launched in 2013 which aims to systematically collect, categorise, analyse and share innovative practices from across the public sector via an online interactive database.[80] Three action lines are being developed: mapping innovative practices through collecting and analysing examples of implemented innovations in the public sector; assessing results by collecting, analysing and developing methodologies for cost-benefit analysis of innovative practices; and promoting innovative practices by collecting and analysing government frameworks and tools to promote innovation.

2.6.3. Alternative measures of progress

Traditionally, Gross Domestic Product (GDP) has been used to measure economic performance and progress. However, there is growing consensus that GDP is a poor instrument for measuring economic development, let alone social progress. A number of projects have sought to measure progress in a way that includes social and environmental indicators as well as economic ones. In 2009 President Sarkozy set up the Stiglitz-Sen-Fitoussi Commission to look into alternative measures of progress.[81] They reported the need to 'shift emphasis from measuring economic production to measuring people's well being'. A few months later, the UK Office for National Statistics (ONS) announced that it would start measuring subjective well-being to help guide

[78] NESTA, *Measuring innovation*, Policy Briefing, National Endowment for Science, Technology and Arts, London, 2008
[79] Viewed on 21 May 2012, http://www.socialinnovationeurope.eu/tags/metrics
[80] Viewed on 27 May 2012, http://www.oecd.org/document/57/0,3746,en_2649_37405_49086969_1_1_1_37405,00.html
[81] Viewed on 21 May 2012, http://www.stiglitz-sen-fitoussi.fr/en/index.htm

national policy. The ONS has been tasked with choosing several subjective well-being questions to be included in the Integrated Household Survey and used as a composite measure of national well-being.[82] The ONS has now announced its 10 indicators of wellbeing and these will be used to guide attitudinal surveys in the future. Other examples include: the OECD's Global Project on Measuring Progress; the UNDP's Human Development Index (HDI) which benchmarks countries based on a combined measurement of health, education and GDP per capita; and the World Bank's Changing Wealth of Nations project which takes broader social and environmental factors into consideration when assessing 'national accounts'.

2.7. Conclusion

This overview has provided a snapshot of examples of support in areas ranging from finance to measurement and legislation. There is a currently a dearth of knowledge about which policies are most effective at supporting social innovation but what is required is experimentation and learning to help grow the field. The other work packages will cover this ground in more detail and make recommendations for future action.

[82] Viewed on 21 May 2012, http://www.ons.gov.uk/well-being.html

3. Summary Propositions

These ten propositions summarise our analysis of the historical, economic and technological context for the growing interest and importance of social innovation and point to opportunities for social innovation in the coming period.

1. There is a growing mismatch between social and environmental challenges and the institutions tasked with addressing them. There are a number of seemingly intractable social and environmental challenges (generational worklessness, poverty, homelessness, addictions and so on) that existing structures, policies and institutions have failed to address. Existing structures are particularly badly placed to deal with new and growing social and environmental challenges such as climate change, an ageing population and chronic disease. The cost implications of these new and growing social challenges are staggering and pose a threat to the very foundations of the welfare state. Social innovation is needed to help address these social and environmental challenges.

2. The need for social innovation has been brought into sharper focus as a result of the current economic crisis: emerging social needs are placing an ever-increasing burden on public spending, at a time when public budgets are already squeezed.

3. Some have argued that social innovation is necessary in this context: current austerity measures require radical cost cutting and efficiency savings. Radical social innovation is required to help reduce public spending and meet new and emerging social needs. However, we believe that this perspective misunderstands the nature of the current crisis – and is therefore inadequate to resolving it.

4. Since the 1970s wages in Europe have not kept up with economic growth (in the US, household incomes have been falling in real terms). This has led to a problem of final demand that has been offset in the last decade by a massive extension of credit to consumers and increased public sector spending – largely in the form of public sector jobs and welfare payments. Therefore, we argue that the current crisis is the result of longer term structural weaknesses, and not simply a severe downturn, and as such, short term monetary and fiscal measures to stimulate demand are unlikely to restore growth by themselves. This has implications for our understanding of the role of social innovation and the kind of social innovation that will be required in the coming period.

5. We argue that longer-term changes in technology are the context for this crisis. We argue that this crisis marks one of the points of transition from a techno-economic paradigm based on mass production to one based on information and communication technologies. The full deployment of these new technologies promises to modernise all existing industries, institutions and activities – thereby driving the next surge of economic growth and development.

6. The changes brought about by new technologies are also compounded by changes in values, beliefs, attitudes and assumptions. Across Europe and North America in particular, there has been a significant shift towards 'post-modern' or 'post-materialist' values of self-expression, autonomy, quality of life and the desire for participation and psychological self-determination. These changing values are at the root of recent trends such as pro-sumption, social activism and the explosion of activity on the web. New needs and desires lead to new patterns of consumption which in turn drive innovation and shift paradigms.

7. This reading of events is important for two reasons. First, there is a significant opportunity for social innovation during this period of transformation, as old institutions, industries and activities are modernised, reconstituted and re-shaped. Second, paradigm shifting values and technologies will shape the nature and direction of social innovation in the coming period – by providing new tools, objectives and opportunities for social innovation.

8. We can already see the first green shoots of the new paradigm: the emergence of networks as the key organisational structure of the new paradigm; hyper-segmentation of markets or what is often called 'mass customisation'; the hyper-segmentation of units of production and the emergence of small knowledge intensive enterprises (SKIEs) and; energy and the environment as a particularly important source of new innovations. We believe that these trends are interlinking, mutually reinforcing and evident in the social field.

9. New technologies are indeed providing many opportunities for innovation. However, it is not at all guaranteed that the potential of the new paradigm will be fully realised. This depends in part on government action and the policies implemented to support social innovation.

10. There is a range of policy options available to governments. These include the creation of dedicated innovation units, agencies and institutions, new funds and financial instruments, laws and regulations, fiscal incentives, new procurement and commissioning structures and processes and new metrics. Rigorous analysis is needed to identify the most effective policy responses.