California Management Review

SUSTAINABILITY

Understanding Hybrid Organizations

by California Management Review

An interview with Dr. Nardia Haigh, editor of CMR's special issue on hybrid organizations.

INSIGHT | INTERVIEW 15 Jun 2015

Nardia Haigh, University of Massachusetts Boston

> *Dr. Nardia Haigh, Assistant Professor of Management and Marketing at the University of Massachusetts Boston, and Guest Editor of CMR's Special Issue on Hybrid Organizations, discusses the emergence of new forms of socially conscious enterprise and their impact on the business landscape.*

Hybrid organizations are, by nature, hard to define. By incorporating elements from multiple economic sectors into their business models and everyday operations, hybrids often exhibit qualities of both nonprofit and for-profit enterprises. But at the core of any hybrid organization lies a commitment to making positive social or environmental impacts. Whether in response to a lack of traditional sources of philanthropic funding or simply in response to growing demand from a more socially conscious consumer market, these organizations are proliferating rapidly, and are poised to assume a much larger role in the corporate world.

In this installment of the CMR interview series, Dr. Haigh spoke with California Management Review's Senior Editor Gundars Strads about hybrid organizations.

What are hybrid organizations, and what need do they fill?

I like to think of hybrids as being on a spectrum. If you imagine a spectrum with pure nonprofit organizations surviving on philanthropy and grants on one end, and pure forprofit organizations with little or no social mission on the other end, hybrids occupy the intermediate points between them. Hybrids may be nonprofits that earn most or all of their revenue [without support], or they may be forprofits that have a very strong social mission and a business model designed to alleviate a particular social issue be it poverty, education, the environment, or income inequality, just to name a few.

In terms of the need that hybrids fill: over the past few decades, government services and funding for social programs has been reduced, and obtaining grants from foundations has become very competitive. In response, hybrids have emerged as a type of organization that earns part or all of its revenue to support a social mission.

Are hybrids simply an attempt to compensate for the failures of government institutions and market capitalism?

To some degree, I think that hybrid organizations are an attempt to compensate for failures of the government they've certainly emerged as a means to address reduced funding of social programs. Government services also generally seek to meet the needs of the masses, and hybrid organizations tend to operate in more niche markets that are often overlooked or underserved by traditional government funding programs.

But I would say that the aim is now to harness the power that capitalism holds for capturing value from a market, and to use [that power] to create social value. Hybrids are serving a growing market segment, called LOHAS (Lifestyles of Health and Sustainability), and this demographic demands goods and services that are focused on health, the environment, social justice, and sustainable living. That segment is actually worth about $209 billion. So hybrids are also directly serving that market. The hybrid entrepreneurs that I've come into contact with are all incredibly strategic and pragmatic people. They want to prove a point: that the capitalist system can be used to create social value and address social ills while at the same time creating economic value.

Does new legislation (like benefit corporation status) create any unfair legal or tax advantages for hybrid organizations? Is there any reason for conflict amongst the different "points on the spectrum?"

I don't believe so. Registering as a benefit corporation, benefit LLC, or L3C (low profit limited liability company) gives businesses the freedom and legal protection to pursue their own bottom line, and to pursue whatever their own social mission might be. That legislation seeks to protect the social mission by insulating hybrids from things that might sway the company from that mission such as a majority of shareholders seeking to promote profit over the designated social mission, for instance. The legislation can also protect the company from acquisition from a large corporation that, for instance, may have a poor reputation on human rights.

Benefit corporations and similar structures are required to simultaneously promote a material, positive impact on society and the environment, extend accountability, consider the interest of stakeholders, and to publicly report on their social performance against a thirdparty standard. To my knowledge, registering as a benefit corporation or benefit LLC confers the same tax rules as any other corporation or LLC, so there are no specific tax advantages.

When critics see the word “social” attached to a discussion about business, they often assume it to be a stand in for “idealism” or “charity.” What is it about hybrids that distinguishes them from other organizations with purely philanthropic motivations?

Hybrid entrepreneurs aren’t generally looking for philanthropic funds. In many cases, they’re not looking for philanthropy at all; they typically can’t even access [that type of funding], because they’re operating under a forprofit model and can’t apply for grants or put out a call for donations, for example.

Hybrid organizations compensate for the lack of access to philanthropy by being highly attentive to changes in consumer preferences. In many ways, hybrids can be seen as a response to a more discerning market and quite a strategic move, in that way. There is also a healthy appetite for investing in hybrids; the market for socially responsible investing these days is worth about $3 trillion, around 12% of managed funds in the United States. And investors are interested in funding organizations that adopt a new approach to creating social impact and financial returns. These investors are certainly looking for a [financial] return, but understand that it might have a longer lead time than other types of venture investment.

Can hybrid organizations grow or scale beyond specialty and niche markets? Or will they always be relegated to the periphery of mainstream corporate activity?

It is true that many hybrids operate in niche markets that are underserved. The concept of “scaling” in these markets may actually [be more akin to] replicating successful niche activity in other markets or locations. For some hybrid organizations, scaling is accomplished through dissemination; they make their solutions, messages, and related intellectual property freely available to the public. One example of this is Mozilla Foundation, which makes its code for the Firefox web browser freely available as part of an open source model. Many other hybrids choose not to focus on the scale of the organization in a traditional sense number of employees, number of branches, or revenue, for instance. Rather, they look at the scale of their social impact the number of beneficiaries they’re able to serve, and the quality of service that they’d be able to offer to those beneficiaries. So it’s a different take on [the concept of] scale.

However, certain other hybrid organizations can, and in fact are, being scaled in much the same way as traditional companies. They are already in the mainstream and competing headtohead with other prominent companies. One of the articles in the special issue, by [Matthew Lee and Jason Jay], explored how hybrid companies have been received by mainstream companies. And those responses range from acquisition, to partnering, to pure competition. One example is Toms shoes, a very well known company based in the U.S.

With regards to partnerships between established corporations and hybrid organizations, is this more than just a PR or CSR effort on the part of the larger organizations?

It really depends on the leadership of the corporation, what they're hoping to achieve, and what the market is demanding of them. [Partnerships offer] mutual benefits; it can be an effective way for the hybrid to scale, and a way for traditional corporations to move beyond conventional PR or CSR goals, which often involve donation to charity, or providing time for their workers to volunteer.

For companies looking to move beyond their current CSR efforts, to achieve a more complete understanding of some of the issues to which they may just be donating at the moment, I would definitely advocate partnering with a hybrid.

What factors are critical to the success of a hybrid organization?

Hybrid organizations that closely align social mission with profit, and also feature a relatively simple value chain, are more likely to be sustainable in the long term. Also, it is important for hybrid entrepreneurs to learn to identify both the positive and negative impacts of conducting their businesses. Many businesses will have not only some kind of positive impact, but also some unintended impacts as well. There's an article by [Diane Holt and David Littlewood] that helps entrepreneurs identify all of those impacts and find ways to address the negative ones while leveraging the positive ones.

Is there any particular advice you'd give to someone interested in starting a hybrid organization?

I think that this could potentially be a very long list! So I'll try to keep it to three short points.

The first would be to define your purpose and unique value proposition. It's so important that the purpose of the business be clearly articulated at the start. The purpose guides the creation of the initial hybrid business model and also guides the business model as it is tested through various stages of growth. It's often this clearly defined purpose and the corresponding social and environmental benefits that allow social ventures and hybrid organizations to leverage multiple streams of value, and to create more interesting and more innovative models.

The second piece of advice would be to define the financial sustainability model. Without money, there is no mission. So that includes the traditional revenue model customers paying for products and services as well as the funding model, whether it's individuals or organizations contributing initial capital, social impact investors, or something else. Or, if you decide to operate on the nonprofit end of the spectrum, determining exactly where those funds would come from.

The final thing would be to define your impact, and how you plan to measure and track that impact. It is important to be very clear about the direct outcome you're aiming to create, and to measure consistently in order to determine whether or not you're being effective in pursuing your purpose and fulfilling that particular value proposition. Aligning direct outcomes with key indicators that can be assessed over time can allow the organization to engage in realtime learning.
