BIG SOCIETY CAPITAL

SOCIAL INVESTMENT INSIGHTS SERIES

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Growing social enterprise through the holding company model

Groupe SOS – An international case study

Groupe SOS is a holding company for social enterprises. This paper describes the benefits of the holding company model for social enterprises, several cultural factors that enable the model, and the group's approach to growth. It concludes by offering potential implications for the UK social enterprise and social investment sectors

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The Social Investment Insights Series are occasional papers drafted by members of Big Society Capital's team on areas of interest to the social investment market.

Big Society Capital is an independent financial institution with a social mission, set up to help grow the social investment market in the UK, so that charities and social enterprises who want to borrow money, or take on investment, can access the finance they need to do more. Since we were set up in 2012, we have committed nearly £150 million in investments to specialist organisations who lend to charities and social enterprises, and are showing that social investment can work. Over five years we will be capitalised with approximately £600 million - £400 million of public funds from English dormant bank accounts, and £200 million from the four main UK high street banks.

INTRODUCTION

Mention the term 'social enterprise' and the word 'scale' won't be far behind. Despite the fact that social enterprises[1] have high growth expectations, they are often smaller than their counterparts in the conventional SME[2] sector. For instance, UK government research has found that, on average, small social enterprises generated around £650k in turnover, roughly one third less than the turnover of the average conventional SME (which was over £1 million).[3] Collectively, the five thousand Community Interest Companies[4] registered in the UK generate around £900 million in turnover – less than most single FTSE 250 companies.

The small scale of social enterprises often prevents them from enjoying the benefits of larger organisations such as:

- Operational leverage (overhead costs often represent a smaller portion of large businesses)
- Financing advantages (larger organisations can gain 'critical mass' by attracting larger amounts of capital)
- Diversification benefits (large organisations can spread their activities and risk across different sectors and activities)
- Innovation (more diversified businesses can grow via cross-fertilisation between businesses)
- Ability to attract and grow talent (large companies can offer a greater variety of career paths and developmental opportunities)

How might the benefits of smaller innovative organisations be married with the benefits of large-scale organisations? The answer could lie in the social enterprise holding company model.

Groupe SOS, a holding company based in France, has developed an approach to managing social enterprises in a network that acts as a hybrid between a large corporate and independent mission-driven social organisations. Consolidating over 45 businesses into a single group, they run enterprises ranging from hospitals to retail stores to drug rehabilitation centres. The Groupe SOS holding company model 'frees up' social entrepreneurs to focus on running their businesses by pooling common support services behind these ventures into the holding company. In the words of the Chairman and Founder, Jean-Marc Borello, "we want to create a school of fish, not a whale".

[1] For discussion purposes we define social enterprise in line with the UK government (BIS) as those businesses that self-identify as a social enterprise and as a "business with primarily social or environmental objectives, whose surpluses are principally re-invested for that purpose in the business or community, rather than mainly being paid to shareholders and owners"; that they generate at least 25% of their turnover from trading and distribute less than 50% of their profits to owners or shareholders

[2] According to data from Social Enterprise UK, 38% of social enterprises saw an increase in turnover compared with 29% of SMEs in 2012

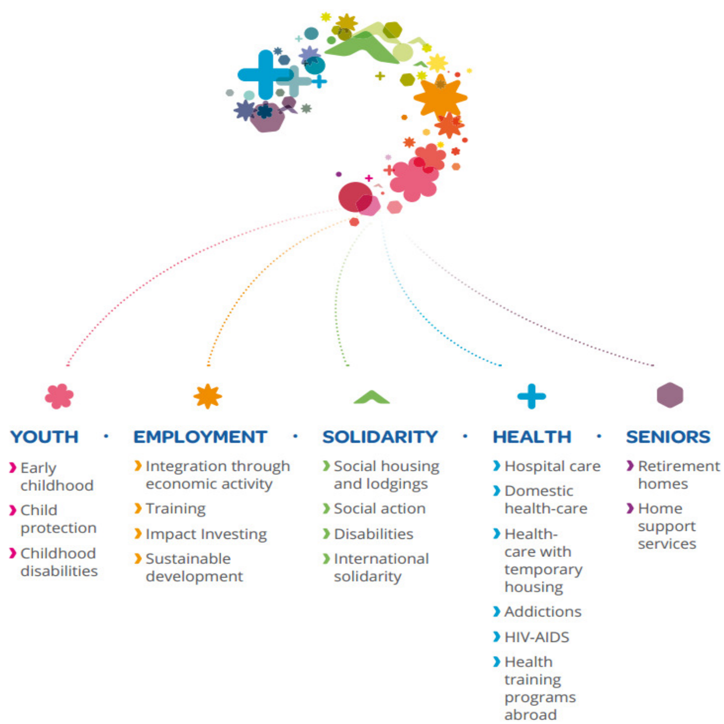
[3] UK BIS Small Business Survey, "Social Enterprise: Market Trends" (May 2013)

[4] A Community Interest Corporation (CIC) is a business with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners. It is perhaps the closest aligned legal form for social enterprise.

THE HOLDING COMPANY MODEL

Operating somewhere between a business association and a wholly owned company, Groupe SOS's federalised management model allows individual social entrepreneurs to gain leverage by accessing professionalised support services and a network of affiliated organisations. The holding company model has enabled Groupe SOS to harness the upsides of networked businesses, growing from a single clinic thirty years ago to generating over £460 million in annual turnover across five core areas (Figure 1). Achieving this scale has been possible by consolidating many social ventures into a charitable holding company, removing many of the common challenges that smaller enterprises often face (Table 1).

Figure 1: Groupe SOS enterprise areas and selected statistics



Groupe SOS in 2013	
Annual turnover	€560 million (£460 million)
Number of beneficiaries	>1 million
Number of employees	>11,000
Number of businesses	>45
Year founded	1984

Table 1: How the holding company addresses challenges faced by small social enterprises

	Common social enterprise challenge	How addressed by holding company structure
Operational leverage	• **High overhead expenses**: Basic operational costs represent a higher portion of income for smaller ventures and erode potential surpluses • **Cost of measurement:** Measuring performance (i.e., non-financial results) can generate additional operational costs unique to social enterprise	• Groupe SOS shares common support functions such as Human Resources, Finance and Operations so that they represent a lower average cost to the enterprise • Groupe SOS has over 400 employees in the head office (out of more than 11,000 employees) providing support to its businesses, of which the largest group is finance/accounting • Subsidiaries benefit from better quality support at the early stage than they would otherwise access, arguably allowing them to reinvest and scale faster
Financing	• **Finance skills:** Lack of finance-specific skills within the enterprise or lack of comprehensive understanding of financing options (i.e., “high searching costs”) • **Available time:** Lack of excess capacity to engage with investors, banks, or other intermediaries • **Access to capital:** Small social enterprises are often perceived as less credit worthy; borrowing is therefore more expensive and harder to find • **Critical mass:** Smaller organisations often lack financial size to justify social investment • **Track record:** Start ups often lack proven interventions or sufficient evidence for investors • **Diversification:** Small social enterprises are usually focused on a small number of interventions or outcome areas, creating potential concentration risk	• The Group houses a dedicated and specialist finance team that works with enterprises to manage the finance and accounting needs of each enterprise • The finance function manages major banking relationships, thus understanding the process and requirements of attracting new funds • Groupe SOS has 30 years of operating experience, credit experience, and relationships with large banks • The finance function at the Group level consolidates funding needs across the Group to create a larger pool of financing need • Groupe SOS has built a track record as a management company rather than at the individual enterprise level – and is able to attract investment at the Group level • Groupe SOS also acquires many types of existing enterprises which have an established track record • Groupe SOS is diversified across five business areas: youth, employment, solidarity, health and seniors
Business development	• **Procurement:** Small social enterprises often fall below the minimum size for contracts with the public or private sector	• Social enterprises can band together through the group structure to compete for larger contracts • The unifying social mission and charitable structure of the group often creates credibility when competing for social service contracts (especially the public sector)
Innovation	• **Investment capital:** Small organisations often lack the excess surpluses required to invest in new businesses, products, etc. • **Risk tolerance:** The higher risk associated with new ventures/products could overwhelm smaller business if unsuccessful	• Investing across the subsidiaries, Groupe SOS can ‘cross-subsidise’ innovation by taking surpluses from more mature businesses and invest in innovations • Groupe SOS can also leverage the knowledge of its existing social enterprises in identifying opportunity and developing models to tackling them (i.e., replication risk may be lower)
People and expertise	• **Access to deep talent pools:** Smaller organisations may struggle to gain visibility and break into diverse talent pools	• Groupe SOS can attract ambitious management talent on a larger scale (with 11,000 employees) • Large network of organisations offers recruits a potential career path and/or more diverse opportunities
	• **Knowledge management:** Smaller organisations must build knowledge predominantly through internal experimentation and external networks	• Groupe SOS holds frequent meetings to share best practice and network • Groupe SOS acts as a support network for building and maintaining knowledge

CULTURAL DIFFERENCES

There are several striking cultural tenets embedded within the Group SOS approach that allow it to thrive, absorbing new businesses and running diverse operations as a confederation.

Perhaps most importantly, Groupe SOS sees itself as a competitive private business that goes head to head with for-profit commercial competitors. Keeping grants or subsidies below 1% of total turnover, Groupe SOS focuses on identifying opportunities in markets with individuals and corporates as purchasers of social value. Its businesses serve more than 300 clients (public and private) including retail consumers. Founder Jean-Marc Borello spends a significant amount of time on the front line where he identifies gaps in social provision that can be addressed through revenue models. In its management approach and performance measurement, Groupe SOS benchmarks itself directly with the private sector.

Despite acting like a private for-profit business, Groupe SOS places a strong emphasis on equality of service provision. Its daycare centres have set aside quotas for deprived customer segments, but the service is undifferentiated from the end users' perspective. Groupe SOS retail shops which act as work integration enterprises, are designed to look and feel just like any another Parisian boutique. And when it evaluates new businesses, Groupe SOS expects no financial subsidies, and instead seeks models that will eventually become self-funding and sustainable.

Third, Groupe SOS views growth as an enhancement of its impact rather than a dilution of its impact. Social impact is not managed in a binary way to the revenue generating activities; it is embedded in the way they work. For instance, its daycare centres work with local authorities to set and regularly review parental surveys and their progress against beneficiary quotas. At many hospitals, they have set aside beds for low-margin but under-served patient groups such as HIV/AIDs patients, the elderly, geriatric care patients. Once patients are released from hospitals, the Groupe has developed a referral programme with other social organisations whereby 'at risk' patients are referred to local social service providers. Generating social impact is embedded throughout their approach to running ventures rather than seen as a siloed activity.

Maintaining an ambition for scale drives Groupe SOS's management approach, evaluation of new opportunities, and the way it integrates generating impact into business models. Thus, Groupe SOS bridges an impact orientation with an eye toward broad service provision and growth potential.

GROWTH AMBITIONS

Since 2002 Groupe SOS has accelerated its diversification and growth, with an average annual growth rate of over 30%. Its expansion has largely been driven by four types of activities:

- **Organic start-ups**: Investments in new entities within the group based on opportunities identified by its founder or other existing social enterprises
- **Acquisitions**: Mergers and acquisitions undertaken by Groupe SOS, including a mix of reactive offers (one of the many proposals received by Groupe SOS each week) and proactive offers (acquisition scans led by the group based on strategic priorities)
- **Distressed or transition ventures:** Organisations which are in financial distress and require immediate turnaround, or could be improved with a different management approach
- **Exiting social entrepreneurs:** Leaders of mission-driven organisations that want to exit the business but secure a mission-aligned owner

In its acquisition activity, Groupe SOS considers both social purpose entities as well as commercial businesses that it can “take social” by adapting the organisation’s mission and operations. For instance, the group recently considered the purchase of one of the country’s largest for-profit hospital chains, a deal under which the group would have tweaked the hospitals’ operations to slightly reduce profitability but dramatically increase the social impact of the hospitals.

The group’s growth has also been buoyed by its social mission and charitable status. When bidding for large social services contracts against financial bidders like private equity firms, the government often favours Groupe SOS as its mission and structure can allay concerns for many purchasers of social services. More recently, the group has seen a surge of acquisition opportunities arising from retiring social entrepreneurs who want to exit the business but ensure that the new owners maintain the social purpose of the organisation.

Groupe SOS has financed its growth with relatively plain vanilla financing – a combination of surpluses and bank debt. Over time, it gradually became easier to borrow as it focused on commercial opportunities without any subsidies. However, more recently, Groupe SOS has attempted to build on its knowledge of operating social enterprises by establishing an externally-facing impact investment fund. Raising €20 million from institutions and retail investors, Groupe SOS is making investments in areas such as healthcare and other high-growth sectors. However, it does not solely make financial investments - the fund draws on the social entrepreneurs within the group to advise on the business, bringing in experts on specific outcome areas. The group has also set up a network of incubators that are mentoring start-ups throughout France, some of which may eventually receive investment from the group’s investment arm. Both the incubators and the fund place Groupe SOS squarely in the centre of innovation while allowing them to harness the skills and expertise from the group that comes from running social ventures on an ongoing basis.

CHALLENGES AND IMPLICATIONS FOR THE UK

Could the holding company model serve as new way of thinking about “scaling” social enterprise in the UK? There are several reasons to think so, but major differences in the UK market structure imply potential challenges. Key questions to consider:

- How does the government’s role as the dominant purchaser of social value change the applicability of a holding company model?
  - Can a holding company create value in delivering government services, or is it better placed to provide mainly private products and services?
  - Is a holding company more or less effective than a potential prime contractor model in the UK?
  - What is the benefit of operating across a large number of sectors when delivering public services on behalf of the government?
- What do the recent failures of Cooperative Group imply for the creation of a social enterprise holding company?
  - The average size of Cooperative Group’s businesses is over £1 billion versus Groupe SOS’s average business size of less than £10 million – to what extent does this difference in size drive differences in the potential for independent governance of each business?
  - To what extent do the challenges faced by the Cooperative Group stem from similar governance structures of a holding company, and how might a holding company be better or worse positioned to drive social enterprise?
- How might the UK shortcut 30 years of development to kickstart a holding company?
  - Would a social enterprise holding company be best placed as an organic start up or acquisition of existing organisations?
  - How does the legal structure of any potential holding company affect its potential for growth?
  - Who is closest to this model (in terms of approach or size) and how can they be supported?
  - Could an existing corporate adopt this approach if it had clear mission locks?
  - What would be the most appropriate way to finance the growth of a holding company?
- What is the role (if any) of international sales and operations in achieving scale for a UK holding company?
  - Nearly 80 per cent of sales by firms in European indices (CAC 40, DAX, FTSE 100) are made outside those countries - to what extent is this required to reach sufficient scale?
  - What is the role of international activities in generating innovation in the UK and clubbing together approaches across multiple countries?

The information and opinions in this report were prepared by Travis Hollingsworth, Strategy and Market Development Director, on behalf of Big Society Capital.

Titles available in the Social Investment Insights Series

Growing social enterprise through the holding company mode: Groupe SOS (June 2014)

The growth of Social Impact Bonds in the UK (coming soon)

The development of the UK Retail Bond market (coming soon)

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