Incubation for social-impact startups

Sudha Srinivasan – CEO N/Core

Here are some indisputable facts - Seed funding available for Indian startups in 2017 was a whopping $191 Million. Over 1200 new startups came up the following year, and 8 achieved unicorn status. Every sector of business is witnessing disruptive innovation the startup way. New business models have emerged to tackle age-old problems, and the best of them have achieved scale with unprecedented pace.

The social sector at large, and the nonprofit sector in particular, has struggled to keep up in this contest for entrepreneurial energy. On one hand, more millennials and post-millennials are seeking purpose early in their careers and looking to apply their skills to meaningful problems.
Many resonate with the need for equitable growth, and the urgency to solve for extreme poverty in our generation and want to contribute in some way. Why then do we see so few of them starting up as nonprofits in the development sector? The answer lies in the sector's structural flaws and gaps in the funding landscape.

An entrepreneur or a start up in the non-profit sector is no different from a for profit startup but funders view them very differently. Take for instance, the various categories of funders in Venture Capital /Private Equity. Each of them - angels, seed funds, Series A or B Venture capital, growth capital funds or buyout funds, have a well understood stage preference, risk appetite and duration of interest. Each knows their place in a larger ecosystem that ensures that top talent and top ideas get the appropriate kind of support required to result in world-class institutions.

The funding ecosystem for nonprofit startups too is beginning to evolve. The structural flaw in the development sector is that the construct of a nonprofit has not allowed for raising, managing and valuing capital. All money inflow into a nonprofit, by way of grants, or revenue from operations, is seen as 'income', and all investment into building highly scalable products, hiring amazing teams, and building awesome partnerships is seen as 'expense'. As a result, donor interest in the past was heavily, almost unilaterally, geared towards operational funding for established organizations, with only a few takers to fund the early stage a startup that is capital intensive. However, in the last few years, we have seen the emergence of social incubators, seed funds and venture philanthropy led by visionary institutions that see the need for innovation and risk capital in the nonprofit space.

How then, can a non-profit raise startup capital?

Beyond bootstrapping, and what can be raised with the help of friends and family, nonprofit founders need funds to validate their theory of change, iterate on their idea and achieve a scalable model or product. Common support systems at this stage are incubators, contests / challenges and crowd funding platforms. While these sources offer small, stage appropriate grants, they are also unrestricted in nature and serve the startup's need for early capital.

The build phase of a nonprofit startup is the most challenging. A startup needs seed capital to build a robust and scalable product, or a technology platform to solve a social problem. The market for seed capital for nonprofits is individual philanthropy. India's largest and most impactful nonprofits that have achieved scale, such as Akshaya Patra and Pratham, had the support of visionary

philanthropists who, like venture capitalists, were willing to place bets on the viability of the idea and the capability of the founder, and saw the multiplicative value of funding their capital needs.

Venture philanthropy is the most powerful way for a HNI/UHNI donor to make their grant go farthest. Their grant can enable disruptive solutions that are significantly more impactful than the prevalent solution and bring to life a high potential nonprofit that will solve the problem at scale.

A nonprofit (by now, an organization, outgrowing its founder-only phase) that has successfully built out its product, and is starting to show positive impact in numbers, is ready for institutional funding to grow its operations. The most stage appropriate donor to build growth capacity is a philanthropic institution or a foundation. Among the most mature donor ecosystems, foundations care deeply about getting the problem solved, and look for high potential for success. While risk appetites vary, they are known to have a very long range view of success and their role in it - and hence will support with funds for talent acquisition, brand and marketing, building fundraising capacity besides funding for product development and operating capacity.

How can a non-profit fund its growing operations?

Nonprofits go where markets cannot go - they serve communities that are excluded by
market-based solutions. The excluded aren't merely the communities that cannot afford to pay for products and services at market rates – they also include communities that require additional handholding and onboarding, resulting in customer acquisition costs far exceeding that for other segments. Hence nonprofits require a proxy customer who will bear the cost of developing

and servicing the needs of this under-served, or un-served audience. Corporate Social Responsibility, or CSR, is the predominant proxy customer – a highly fragmented donor base, with very diverse motivations to give – but nonetheless, one that values results and relationships, and can help successful organizations to grow their impact.

The most powerful way to improve effectiveness and efficiencies of nonprofits is to hold them to similar standards as for-profit collaborators and focus the relationship on achievement of goals at quality, per commitments. If CSR deals are structured in a goal centric manner, with provision for capacity building activities such as ramp-up, learning and development of program teams, build knowledge and partnership networks, run innovation projects etc., then the partnership evolves beyond compliance requirements and helps to build a shared legacy and brand for the corporate as well as for the nonprofit, through results achieved collaboratively.

Incubators like N/Core invest in entrepreneurs and to enhance their capability as well as ambition to grow their idea. Beyond this early stage support, nonprofit entrepreneurs need mission aligned support systems through philanthropy and corporate sponsorship to fuel their work. Eradicating extreme poverty, and closing the gap between our GDP rank (6/181) and HDI rank (131/181) requires disruptive models for change – and we hope that exceptional change makers will get the support of purposeful funding ecosystems to close this gap with a sense of urgency.