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Exploring Impact Investing Models in the Social Economy

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I. Introduction

Since the 2000s, the concept of the “social economy” has gained attention and momentum in Korea. After diverse organizational types such as social enterprises, cooperatives, and social ventures in the West were introduced, Korea was able to prepare and improve relevant laws and regulations, and as a result, social economy organizations have sprouted nationwide and are growing gradually. In the existing discourse of capitalism, the primary purpose of a corporation is profit maximization, whereas in the discourse of social economy, the aforementioned types of corporate organizations aim for the realization of social value as well as profit creation.

The realization of social value means to solve environmental, community, and social problems through the business activities of corporate organizations. It goes beyond the Pareto improvement in the market economy

and contributes to resolving issues in the area in which companies operate. Put differently, social economy organizations not only seek to generate profits but also actively intervene in solving various social problems such as climate crisis, educational disparity, and poverty as members of communities and societies from the perspective of so-called corporate citizenship.

In light of this trend, this study pays attention to so-called impact investing, which makes these social economy organizations sprout and grow. Put simply, impact investing can be defined as the act of investing in a corporate organization that seeks to create both financial and social returns. Unlike traditional financial institutions, which evaluate a company’s business structure and operations only with financial indicators, impact investors provide seed funding to organizations that launch products and services that can solve social problems or make investments for scale-up. Therefore, impact investing is essential for the existence of social

economy organizations, playing an important role in the creation and scale-up of social ventures, and the expansion of the ecosystem as a whole. The purpose of this report is to derive policy suggestions for the sound growth and development of the ecosystem of the Korean social economy by exploring the status of impact investing in Korea.

II. Research Questions and Methods

Based on the above-mentioned research background, purpose, scope and target, this study presents the following research questions:

- How is the Korean social venture policy framework working? How are social ventures institutionalized, evaluated, and supported, and what are their characteristics?
- How is the impact investing ecosystem working in Korea? How do impact investing institutions (equivalent to supply) work, and how do social ventures (equivalent to demand) perceive impact investing?
- What are the policy suggestions for future development, considering the current status of the Korean social venture policy framework and the impact investing ecosystem?

What research methods can be used to answer these questions? First, we examine the policy framework related to social ventures through archival research. Such archival research is significant in that it helps to gather support policies scattered across various government ministries and institutions, and to analyze the strengths and weaknesses of such policies from the perspective of supporting the formation and

development of a social venture ecosystem.

Second, we review the overall impact investing ecosystem through focus group interviews (FGI) and surveys. Surveys are meaningful in that they can show the current status and situation comprehensively like an aerial view, and FGIs are also useful in that they reveal additional information that cannot be identified with statistics and data. For this study, we conducted FGIs with major impact investing institutions in Korea, and used each institution's public annual report and structured questionnaire to have an in-depth interview with the CEO or officials from each institution. Key issues were identified during the interview process, followed by the examination and analysis of the actual status and situation regarding those issues.

III. Korea's Policy Framework for Social Ventures

This section examines the policy framework for social ventures through archival research, focusing on social ventures, but also including social enterprises. First, it deals with the naming of social ventures, the incorporation of the Act on Venture Businesses, the introduction and revision of social venture identification standards, the introduction of the social venture valuation model, and the institutionalization of Social Value Index (SVI). Second, it focuses on social venture promotion policies, exploring start-up support, initial support, nurturing support institutions, general support for ventures (TIPS: Tech Incubator Program for Startups) including social ventures, and comprehensive start-up support system. Third, it also deals with the social enterprise promotion policies and reviews the Social Enterprise Promotion Act, Seoul

Metropolitan Government's policy for fostering social enterprises and its support for starting social enterprises.

Combining the archival research results, we can see the characteristics of Korea's policy framework for social ventures. It is the control and intervention of a strong state, or a developmental state. Development state theory is a discourse that confirms and emphasizes the importance of the national industrial policy, which provided the driving force that led the beginning, growth, and development of high value-added industries based on the intervention and control of the powerful bureaucracy during the period of high growth in East Asian countries (Amsden, 1992; Evans, 1995). After tracing the formation and change of the policy framework for social ventures, it was found that the development state model still exerts a certain power in private sector-led open innovation such as social ventures. The institutionalization process which involves naming, identifying, categorizing, and systematizing social ventures and incorporating them as policy targets can be seen as a typical example of policy enforcement of a development state. Entrepreneurs who had previously started or operated a social venture freely in the private sector now have to pass the criteria set by the government (the Ministry of SMEs and Startups) and a public institution (Korea Technology Finance Corporation) to be recognized as a "social venture" and receive related policy support. In this regard, there are several points where Korea's social economy promotion policy can be interpreted as a progressive form of "Saemaul Undong."

This also applies to the policies on social enterprise certification as well as other related policies. Even in the realm of social innovation and social economy that pursues bottom-up changes, the process of setting and categorizing policy targets is top-down, and various

public support is connected here.

In such a state-led policy framework for social ventures, the division of roles of administrative ministries is noticeable. Depending on the type of social economy organization, social enterprises are supervised by the Ministry of Employment and Labor, cooperatives by the Ministry of Economy and Finance, village enterprises by the Ministry of the Interior and Safety, self-support enterprises by the Ministry of Health and Welfare, and social ventures by the Ministry of SMEs and Startups. Also, the accreditation and certification procedures for legal personality and related support are intertwined according to the relevant ministries. Hence, public interest and support can only be received if these organizations are included in a tightly designed network from the point of view of law and regulation, not from the point of view of business and social innovation.

Such state-led institutionalization and support may help social ventures sprout, but in the long run, have a high risk of suffocating and limiting social imagination, which is the core and basis of social innovation and social entrepreneurship. Moreover, the state-led approach is inflexible by itself so it can hinder so-called disruptive innovation. For example, the existing social venture evaluation system evaluates social and innovative characteristics of the manufacturing (M) sector and those of the service (S) sector separately. This means some creative business models established through multidisciplinary and multisector collaboration can span several industries thus may not be able to come under this dichotomous evaluation system, being placed in a gray area. In addition, rather than the state intervening in the formation of incentives for establishment and growth of social ventures, which may lead to the selection of an organizational form and structure suitable for the type and content of the

business, there is a higher risk of distortion that causes new ventures to select a specific organizational type and structure to receive the necessary public support as they go through the critical initial phase called “the death valley curve” between the foundation and survival.

From a philosophical approach, it can be explained with Habermas’ colonization thesis and Weber’s iron cage thesis. Habermas said that systems such as the economic system (market) and the administrative system (state) gradually and systematically invade and colonize the lifeworld of the private and public spheres, and Weber explained that a bureaucracy based on rationalization could become an iron cage which restricts human beings. Both these can be a description of a development state’s policy framework. Since the creative social entrepreneurship emerging from the lifeworld can survive only when it is invaded by the naming, identifying, and support of the administrative system, and support can only be received when social and innovative characteristics of social ventures are quantified and compared in the name of rationalization, it can be said that the state-led policy framework is an empirical example of lifeworld colonization and the iron cage of bureaucracy and rationality.

Although there would be several cases where individual companies can survive and create an inflection point of growth through government support, the birth and formation of such a policy framework has its own set of risks from the point of view of the ecosystem as a whole, and the differing policy support for social economy organizations by legal personality owing to the division of roles of administrative ministries is highly likely to cause distortion of social entrepreneurship. To resolve this, the role of the private sector needs to be strengthened, and the impact investing ecosystem, which will be described later, has

a particularly important meaning in this regard.

IV. Korea’s Impact Investing Ecosystem

This section explored the impact investing ecosystem in Korea. In particular, the concept of “impact venture” was proposed to include not only social ventures and social enterprises, which are the main targets of impact investing, but also general ventures with impact orientation. It provides an overview of the impact investing ecosystem in Korea and presents and analyzes the survey results on major impact investing institutions that correspond to the supply side and on impact ventures that correspond to the demand side.

1. Increasing Knowledge and Understanding of Impact Investing

This section introduces the concept of “impact” and “impact investing” based on global consensus. After examining the opinions of impact investors and impact ventures, it was realized that these concepts need to be clearly established according to the Korean context and circumstances for the future. It would be crucial for everyone involved to have the same or almost similar conceptual understanding of the words “impact” or “impact investing” by sharing the definition with impact ventures and impact investors. Without establishing these concepts firmly now, unnecessary misunderstandings and conflicts are highly likely to occur, and communication costs to resolve them are also likely to increase. In particular, problems may arise in the partnership between impact investors and impact ventures, which can eventually lead to inefficiency at the ecosystem level, so efforts in this regard are urgently

needed.

In addition, it was found that an influx of ordinary investors is occurring in the process of the growth of the impact investing market, and many of them are likely to lack understanding of social values or impact, or have their own prejudices. To solve this issue, it is necessary to provide separate education, seminars or workshops for general investors who want policy finance related to impact investing. Impact ventures do not have enough time to focus on their business, and it would be too much of a burden if they have to explain the meaning of impact and persuade them of the prospects.

In addition, as civil society, public, and media interest in impact investing is growing, it is becoming increasingly important to deliver accurate information to them in an easy-to-understand manner. In this regard, it is judged that cooperation with academia is necessary. In particular, the Korean Academic Society of Business Administration (KASBA), which represents the Korean business academia, has shown high interest in social value and impact, especially in the leadership group, including the current president (Professor Sang-Man Han of Sungkyunkwan University) and the next president (Professor Jae-Goo Kim of Myongji University, former president of Korea Social Enterprise Promotion Agency). Also, under the leadership of the KASBA, business scholars from various departments have gathered to form the Korea Business Roundtable (KBR) and are actively conducting research and educational activities. If such an organization can be utilized, it is possible to obtain help in research for re-establishing the concept of impact and impact investing, launching related educational programs, and raising public awareness.

2. Role of Impact Investors

The perspective towards impact may differ from person to person. Therefore, impact investors need to discuss the concept of impact with impact ventures by having sufficient communication and objectify it as much as possible through operational definition. In addition, it is necessary to agree in advance on what indicators will be used and when and how to measure them.

Some of the impact ventures were concerned that impact investors tend to place excessive emphasis on scale-up, which is the quantitative aspect of business model and impact. Of course, it is self-evident that general investors take risks when they can ensure financial performance improvement and return on investment through rapid growth. However, since impact investors pursue both financial and social performance, the importance of business models and scale-up also needs to be understood in connection with the possibility of enhancing social performance. Also, in this process, it is necessary to remember that the beneficiary group of social performance is generally those with low purchasing power, and to consider the quality of impact, that is, the importance of scale-deep. In the end, impact ventures and impact investors will need to contemplate how to balance financial and social performance together and try to find the best answer at each point.

In addition, impact investors need to strengthen impact accelerating support for impact ventures, such as providing necessary technical support and networking. From the perspective of the government or funding agencies in charge of policy finance, it would also be helpful to focus on this aspect and consider how impact ventures can take a balanced approach in terms

of pursuing quantitative scale-up and qualitative scale-deep.

Impact investors need to think about how to make a better impact, rather than becoming overly affected by impact measurement results. If there is an aspect where the impact has not been created as expected, it is necessary to have a partnership to analyze the cause and find a solution together. If the lessons and implications drawn in this process can be shared in the form of documents or through workshops or seminars, it will be of great help to the development of Korea's impact ecosystem.

3. Role of Impact Ventures

Impact ventures need to make efforts to define, interpret, measure and evaluate the impact so that the impact they are making can be explained in the best way. To this end, it is necessary to clarify what social problems they are trying to solve and what social values they are pursuing, and to reflect and document them in their social mission.

In addition, by sufficiently analyzing the innovation, market size, financial feasibility, financial/social sustainability, and scalability of the solutions designed to solve the designated social problems, they will have to increase efforts to strengthen capacity in "impact communication," providing easy-to-understand and efficient explanations to internal and external stakeholders including impact investors.

Finally, it is important to conceptualize the impact that occurs through the execution of the solution, and thoroughly design in advance the "impact measurement and management," including the selection of indicators to measure the impact, and the decision on measurement methods and time.

Although carrying out these activities continuously requires understanding and learning about impact measurement and management on the part of internal members, Korea's impact ecosystem has not sufficiently met these needs. In this regard, the government, public institutions and non-profit foundations will be able to play a role. In particular, if the educational contents on the above topics are prepared and accumulated in the form of documents or videos and shared in the form of public goods, it will help prevent wastage of resources and pursue common development at the impact ecosystem level. Some excellent examples include the social value content platform produced and shared by the Center for Social value Enhancement Studies (CSES) and the ESG content platform produced and shared by the Korea Chamber of Commerce & Industry (KCCI).

Recently, concerns about the use of impact for publicity and about the risks of impact washing are increasing. The two are considered a significant risk factor for impact ventures. To solve this problem, it is necessary for impact ventures to clarify the social value they pursue, measure the impact created by their solution objectively and conservatively, and share the results with stakeholders. In particular, the trust and support of other members of society can be gained only when impact ventures, instead of hiding their shortcomings, reveal them and seek the wisdom, help, and cooperation of others, and show willingness to do better together. Thus, by making good use of the impact measurement and management system, the sincerity of impact ventures can be recognized by other members of society.

V. Policy Suggestions: Introduction of the Social Impact Assessment and Customized Policies for Impact Investing

1. An Integrated Approach to Social Economy and Introduction of the Social Impact Assessment

First, as discussed above, social enterprises are currently supervised by the Ministry of Employment and Labor, cooperatives by the Ministry of Economy and Finance, village enterprises by the Ministry of the Interior and Safety, self-support enterprises by the Ministry of Health and Welfare, and social ventures by the Ministry of SMEs and Startups. A critical approach is needed to review the current designation of competent ministries and formulation of related policies based on the type of organization. In other words, rather than focusing on the organizational form and legal personality, it is recommended to establish a standard focusing on the social and innovative nature of the organization itself, and introduce the Social Impact Assessment (tentative) which will be operated from an integrated perspective.

Prejudices and biases based on the division of non-profit and for-profit organizations, as well as the designation of competent ministries and formulation of related policies based on the type of organizations are causing dangerous market distortions. For example, in the field of social economy, some newly-established general cooperatives are receiving social enterprise certification in order to enjoy related benefits, and are applying for support from both the public sector including the central government and local governments and the private sector that supports the social economy. This means that entities and organizations that are

skillful in using multiple identities are relatively more advantageous in receiving policy support, while those that are not updated with the latest information are likely to be marginalized or excluded. Furthermore, some entrepreneurs who have started a general venture may apply for related support after adding some social elements to their business model in order to receive benefits related to social ventures.

In summary, as various policy supports become available for different types of organization, market distortions and unnecessary identity politics are taking place by drawing lines and setting boundaries. This is why an integrated approach to the social economy is needed even more.

As a way to solve the above issue, it is suggested to establish an evaluation system that quantifies the increase in positive externality or decrease in negative externality of the same amount as the social value created by various organizational types, and to link this with support measures. Through such an evaluation system, regardless of the type of organization, if an organization creates meaningful social value, it can be recognized and supported. Rather than determining the eligibility for policy support by categorizing organizations according to their type, it would be desirable to link policy support with the social value and ripple effect of the business model, which will also serve to address the issue of equity between organizations. In other words, such an evaluation system can contribute to solving the problems of discrimination and overlapping support between various legal personality and entities of the so-called social economy, such as social enterprises, social ventures, and social cooperatives.

In this regard, it is recommended to introduce the so-called Social Impact Assessment, similar to the Employment Impact Assessment or the Environmental

Impact Assessment, to diagnose and assess the social and innovative nature of the organization itself and link the assessment results with policy support, breaking away from the designation of competent ministries and formulation of related policies based on the type of organization. An organization that can act as a policy coordinator for multiple ministries, rather than individual ministries, would be appropriate as the entity responsible for the Social Impact Assessment. In addition, to care for the organizations that are not familiar with performance measurement and evaluation under the evidence-based policy support system, it will be necessary to maintain certain parts of the existing support system for each type of organization and provide education related to performance measurement and evaluation.

2. Customized Policies to Promote Impact Investing

If the above-mentioned policy suggestions are for the entire Korean social economy, what specifically is needed for the development of the impact investing ecosystem in Korea? Above all, the most important role of the government is to basically invest in people and institutions (infrastructure). And, the key role of the private sector is to present a new model through social innovation (impact ventures) and to continuously invest in promising impact ventures to create meaningful social value (impact investors). In other words, it is important to properly divide the roles between the public and private sectors.

More specifically, it is expected that the impact investing ecosystem in Korea will take a further leap forward through diverse measures such as tax benefits, system improvement, promotion of non-profit and financial ecosystem participation, support for impact investing institutions, and participation in public funds.