

“Development of the impact investing ecosystem in Ukraine”

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DEVELOPMENT OF THE IMPACT INVESTING ECOSYSTEM IN UKRAINE

Abstract

The impact investing ecosystem is currently in its infancy in Ukraine. The aim of the paper is to identify the problems of impact investing development in Ukraine and to propose the ways to develop the ecosystem of social investment in the country. In the course of the research, general scientific methods of analysis were used: formal, logical, and comparative. Results of the research suggest that theory and practice of state regulation in Ukraine still lack the conceptualized mechanisms of impact investing and the corresponding institutional environment. On the other hand, there is a high level of interest and engagement in it from both the public and potential and current investors. The data obtained prove the importance of civil society cooperation in creating a favorable ecosystem of impact investing to maximize its integration into the economy. The development of impact investing ecosystem in Ukraine depends on certain socio-economic and legal barriers at an initial stage such as: low level of public understanding about the problem, absence of clear legal regulation and uncertainty of the "rules of the game" at the legislative level, openness and publicity of enterprises, which is not a characteristic feature of the economic environment in the country today. Furthermore, effective directions and mechanisms for development of the impact investing ecosystem are proposed.

Keywords

ecosystem, impact investing, social investments, social responsibility, social entrepreneurship

JEL Classification

A14, D64, D71

INTRODUCTION

The phenomenon of socially responsible business is not anything totally new for Ukraine, where entrepreneurial mechanisms have been created to operate actively and to generate profit and influence on the social infrastructure in the country within the past ten years. Social entrepreneurship in Ukraine is increasingly acquiring a combination of commercial component and philanthropy.

However, today the concept of impact investment is still evolving in the country. The transfer of prevailing stratagems of social entrepreneurship to the sphere of impact investing in Ukraine can be the significant contribution to the development of welfare of the country.

The experience of foreign countries shows that the practice of impact investing contributes not only to the development of a significant social effect, but also to a tangible financial profit.

Thus, the research problem is stated as follows: Is impact investing able to establish a stable social investment ecosystem in Ukraine? The current paper aims are:

- to determine the role and tasks of impact investing in the country;
- to propose possible solutions to the issue of establishing a stable social investment ecosystem at an early stage;

- to determine the specific features of impact investing, separating the notion of general investment;
- to identify the relationship between the concepts of “innovation”, “social entrepreneurship”, “social project” and “impact investing”;
- to identify the problems of impact investing development in Ukraine;
- to recommend the ways to develop the ecosystem of impact investing in Ukraine.

In the course of the research, general scientific methods of analysis were used: formal, logical, and comparative; general methods: abstraction and generalization, idealization, analogy and modeling methods; as well as empirical methods: secondary sociological analysis, analysis of regulatory documents; institutional, inductive and deductive approaches were applied.

Today the main directions of the development of the ecosystem of impact investing in Ukraine should be the traditional mechanisms of social security, as well as comparatively new directions, such as supporting the activities of specialized social investment institutions and the development of promising impact investing sectors. Hence, the findings of the study represent the importance of the development of impact investing in Ukraine, citing a number of social and economic challenges that can be addressed in the course of voluntary initiatives and state support.

1. THEORETICAL BASIS

To compare the indicators of the development of impact investing in Ukraine and other countries, the comparative analysis was used. The logical and analytical methods were used when proposing the recommendations for the development of a stable ecosystem of impact investing in Ukraine, taking into account the present situation of the studied object in the country and suggesting the plans and directions for the development of impact investing in the country.

As a result of generalization and abstraction, essential issues of the object have been synthesized and subsequently identified. By means of idealization, the desired absolute limit of development of the impact investing ecosystem in Ukraine was determined, which subsequently made it possible to construct the abstract schemes of real processes of the studied object.

The following empirical methods have been used in the research: secondary sociological analysis as a resumed analysis of the data of previous studies with a view of a new research approach, which allowed to verify the research results and to cumulate the sociological information received a previously; analysis of regulatory documents when studying and analyzing the legal regulation and public administration in the field of impact investing in Ukraine; institutional, inductive and

deductive approaches were applied as a forms of organization of multidisciplinary research, in particular the classical direction with the study of organizations and formal legal norms governing the relations between people in society as institutional objects, as well as social norms formed by social systems, and setting patterns of social behavior.

2. RESULTS

Under uncertainty of an explicit endorsement for social entrepreneurship, as well as for impact investing at the state level in Ukraine, the importance of civil society cooperation in creating a favorable ecosystem of impact investing to maximize its integration into the economy and the society of the whole country is significantly higher.

Impact investing can be also considered as an instrument of corporate social responsibility of enterprises, because it is aimed at implementing the social programs.

According to the Global Impact Investing Network (GIIN, 2017) – an international network of social investors founded in 2009, which comprises more than 2000, individual investors and companies today – financial contributions to the sphere of impact investing in 2016 accounted for USD 114 billion all over the world, but mostly in U.S. and Canada (46%), WNS Europe (Western, Northern,

Source: Global Impact Investing Network (2017).

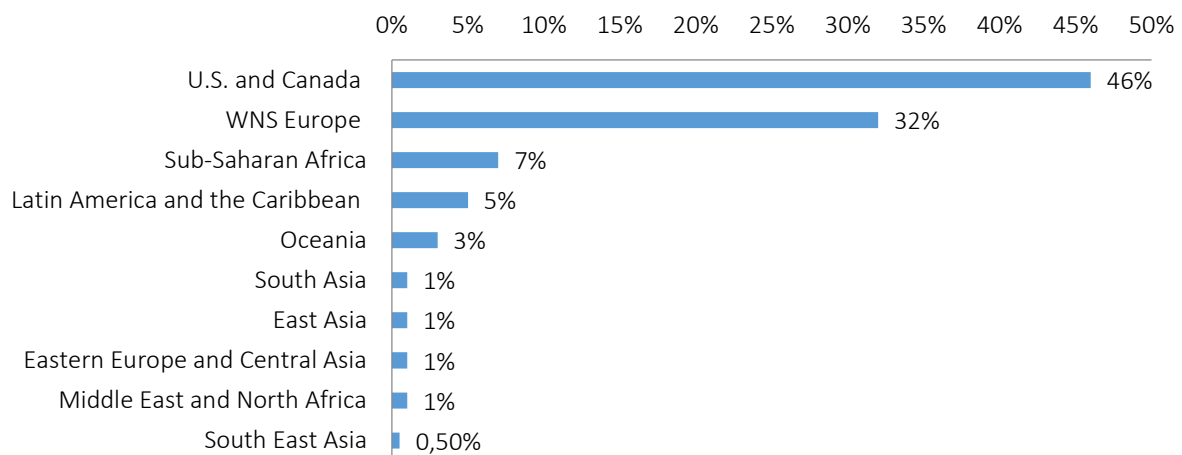


Figure 1. Geographical location of social investors (headquarters) under the GIIN review

and Southern Europe) (32%), Sub-Saharan Africa (7%) and Latin America and the Caribbean (5%), due owing to the list of respondents (209) of the GIIN's Annual Impact Investor Survey 2017 (Figure 1).

Possible way to address the issue of creation of a stable social investment ecosystem at the initial stage is to diversify the attraction of public initiatives as a gratuitous act of charity in the most diverse areas of support:

- free counseling;
- representation of social projects and social entrepreneurship in the public service;
- provision of legal assistance;
- provision of information support in the mass media;
- development and administration of networks and websites for social projects;
- marketing services (first of all, market analysis and promotion of a product or service of a social project);
- rent-free provision of premises for marketing the product or service of a social project;
- institutional services and logistical support: complex service of fair organization of business meetings, negotiations; organization of

the participation of SMEs social projects in exhibitions, seminars and conferences and so forth.

It is clear that social investments play a decisive role in the life of society, because their size directly affects the level and quality of human life.

Nevertheless, the main goal of social investment should be the development and efficiency of the national economy, as it is the material basis for solving further social issues.

Under the state's socially – oriented economy, almost all investments in the economy's development can be considered social, they can be directly aimed at meeting at solving needs or indirectly at solving social issues as a result of economically-directed investments with a multiplicative mechanism of influence on the welfare of society through the increase of economic indicators of the state.

In this context, the following types of impact investing can be identified:

- economic and social investments directed to the service sectors of the national economy;
- direct social investments.

It is also advisable to classify the impact investing according to the criterion of their subjects or sources, which may include the state, commer-

cial enterprises, non-profit organizations (national and international) and individuals. Thus, the following types of social investments can be distinguished:

- social investments financed by the state;
- social investments financed by the commercial sector;
- social investments financed by national and international non-profit organizations;
- social investments financed by individuals;
- social investments with combined sources.

An ideal variant to support and to develop the social entrepreneurship in the process of social investment ecosystem formation is the combination of a social project with a financial model through which the commercial part of the project provides free of charge one. Thus, social projects are guaranteed by giving the particular potential investors' attention.

Today, it can also be observed that the business community in Ukraine is increasingly drawing attention to social projects. Thus, participation in realization of different social projects has increasingly drawn the attention of business sector of the country. Particularly it is expressed in venture investment and social investing, which, moreover, increasingly tend to be integrated. Therefore, a new concept of venture philanthropy appears, which implies a high level of attracting venture capital to the process of selling the product of the social project.

Indeed, today the sphere of social projects receives a greater response from the private sector of Ukraine, nevertheless, in a crisis economic situation, such a financial model cannot be considered stable. This led to a rethinking of approaches to the implementation of private social projects in the country and gave impetus to the development of social entrepreneurship in Ukraine.

The successful social businesses in Ukraine, which also have experience in attracting social investment – networks of public restaurants, the salons of visually impaired and blind masseurs, busi-

nesses engaging to work unprotected and affected segment of the population, production of souvenir items with national symbols – can be cited as examples.

In practice, the sides of such combinations (social project with a financial model) can face certain difficulties, because venture financing is usually provided for a definite period of time. At the same time, social issues that require solutions are usually of a long-term nature. In the end, in such circumstances, social enterprises, initiating a social project, must constantly spend time and efforts to find new investors. On the other hand, social investors are interested and invest in the specific activity of the enterprise, which constitutes only a small part of the entire activity of the organization.

Another problem is that investors want to finance their field of activity or invest in the financing of significant tangible assets (which makes them more visible). For example, most funds seek to finance the launch of new approaches to solve social problems. Then, they are perceived as organizations with creative thinking, champions in the field of social innovation. However, after launching the project, they often lose interest in financing further activities (Kickul et al., 2013).

This is the main difference between social investment and capital expenditure – in conditions and destination positions of investment funds. After all, investments are focused on the return of funds within a certain pre-determined time, meanwhile, a significant part of investments in socially-oriented projects is formed on free and irrevocable basis, along the line of harmonization of interests and values of all participants of the investment process, as well as consumers, whose interests become the priority goals of social investment.

In addition, there are also traditional forms of charity: government grants, fund grants, individual donations and various receipts from enterprises. Obtaining such types of investment, social enterprises are required to provide appropriate reporting on the use of invested funds, economic efficiency and social benefits received. Therefore, only non-profit social projects can count on such traditional forms of charity, since tax credit for charitable donations applies to them (as opposed

to commercial organizations). Moreover, in accordance with the general rules of charitable foundations, investment in commercial institutions is considered undesirable, even if they carry out social projects activities (Kickul & Thomas, 2012).

Thus, the subject of social investment is given a specific feature at the very initial stage of the social project, refusing to receive direct benefit from the project implementation in favor of the consumer social product or service.

In view of the foregoing, it should be noted that social entrepreneurship is a prerequisite and consequence of the social project as a phenomenon of economic reality, in essence, social entrepreneurship is in itself a social project in its broadest sense.

The basic principle of the successful functioning of social projects is the individual initiation of participants in social and societal transformation projects supported by the theoretical principles for restoring spent organizational energy in the process of developing a synergistic effect and corresponding practical developments expressed in the resulting social effect. After all, the necessary condition for the activities of any organization is to follow the law of development, which requires not only the generation of the amount of energy recovering the energy expended, but also the release of free energy, directly providing the functioning of the organization – thus, a social impact is produced. In this context, understand the term “a part of social transformation projects, giving impetus to the development of social entrepreneurship”.

Another characteristic feature of a social project with the participation of social investors in particular is the specific motivation expressed in the public recognition of the project participant and is one of their marketing objectives. In addition, social investment also has other benefits:

- creating a favorable image of the investor as socially responsible, raising the level of recognition, developing a positive reputation in the society;
- long-term prospects for the investor’s business – a natural reaction to improve the attitude of the society towards socially responsible com-

panies that are associated with charitable authoritative institutions;

- the influx of highly skilled personnel as a result of a positive image of the social investor;
- wider access to attracting diverse resources;
- an increase in the incomes of social investors as a result of the above mentioned factors. For example, the social responsibility of the investor company sooner or later contributes to the increase in the price of its shares. In the stock market, a socially responsible company will be considered a company with less risk and more open to social commentary;
- possible tax breaks, reduction of pressure from the public authorities.

Today impact investing is an exciting and rapidly growing industry powered by a variety of investors, which can be private equities, angel investors, corporate investors, venture capital, non-government organizations, different social funds and financial institutions. Reputed social investors can be mentioned: Ashoka: Innovators for the Public, Rockefeller Foundation, Bill & Melinda Gates Foundation, Gatsby Charitable Foundation, JP Morgan, South Africa PIC, Acumen Fund, Bridges Ventures, Elevar Equity, Ariya Capital, The Foundation for Social Entrepreneurs, Big Society Capital, Accion International, Charity Bank, Swiss Investment Fund for Emerging Markets, Deutsche Bank.

The world authoritative body in the field of impact investing, inter alia, is United Nations Development Programme, which has been very active in Ukraine over the past ten years. Ongoing UNDP projects are worth summarizing here.

Thus, individual investors or organizations and institutions that systematically invest in social projects and social enterprises in order to develop a social effect and obtain commercial income (in part, as an option) should be considered as social investors. Also, social investment is becoming an increasingly attractive sector for both government agencies and large commercial backgrounds, as well as highly specialized funds and

Table 1. Ongoing impact investment projects of the United Nations Development Programme in Ukraine

Source: Adapted from the United Nations Development Programme (2019).

Project name	Project goals	Expected results, accomplishments	Timeframe	Focus area	Amount contributed	Donor name
European Union/ United Nations Development Programme “Combining homeowners to implement sustainable energy-efficient solutions” project	To improve the energy efficiency of the residential sector in Ukraine and to reduce greenhouse gas emissions	At least 2,000 new condominiums should be created. At least 4,000 condominiums (both new and existing) should receive assistance through training and consultations. At least 480,000 Ukrainian people should gain directly from the project. At least one million people should have an interest in energy efficiency.	October 2018 – September 2020	24 regions of Ukraine	EUR 4 million	European Union
Sustainable development of rural areas of Chernivtsi and Odesa regions	To contribute to the well- being of the most deprived population of two regions of Ukraine	Strengthening public monitoring of structures and procedures that influence local decision-making authorities. Improving the skills of civil society cooperation in its relations with local authorities. Enhancing the development of agricultural cooperatives, providing small grants to communities intending to set up agricultural cooperatives.	April 2014 – September 2019	Inclusive growth; democratic governance	USD 29,715,034	Austrian Development Agency; United Nations Development Programme; European Commission; Adam Smith International
Support Ukrainian Parliament engagement on the issues of sustainable energy and environment	The implementation of a number of environmental reforms as a priority for Ukraine	The functioning of the Ukrainian Parliament in the field of sustainable energy and environment should be improved through the creation of new authorized body. Raising the level of information support for environmental issues.	July 2018 – June 2020	Inclusive growth	USD 556,111	Sweden
Preventing growing tuberculosis and HIV/AIDS in Ukraine	To promote the capacity of public authorities of Ukraine to prevent growing tuberculosis and HIV/AIDS	Follow-up appointments of competent public authorities to the regions of distribution of tuberculosis and HIV/AIDS on a regular basis and according to previously developed and approved annual work plans.	December 2012 – December 2019	Basic services	USD 648,917	Global Fund To Fight Aids
Provision of services to the Ministry of Health of Ukraine for organizing and conducting procurement procedures	Procurement of medicines through international organizations as a temporary solution until 2020	Development of an electronic system for managing stocks of medicines and medical devices. Purchase of life-saving drugs according to the long-termed agreements.	November 2015 – December 2019	Basic services	USD 402,507,425	Ministry of Health of Ukraine; United Nations Development Programme; Government of Turkey

large companies.

In general, the most popular impact investment tools are buying a stake in perspective companies and various types of loans. Most of the impact investment goes to the social business in the stages of a start-up or venture, when there is a final value-added product, but mass production has not been launched yet.

At the moment, the most universal impact investment tool is so-called “green” bonds. In 2012 their volume amounted to USD 2.6 billion, in 2015 – 42 billion, and according to the results of 2017 – 200 billion. The main issuer of “green” bonds is the World Bank. Another example of a mass social in-

vestment product is the bonds of the NCO Calvert Foundation from the USA. Anyone can buy these papers for USD 25. The collected money (USD 318 million as of September 2017) is invested in various social enterprises and programs.

In the European countries, impact investing has been a major concern for pension funds in recent years. At the same time, the initiators of such deposits are usually the beneficiaries – the fund depositors themselves. For example, in the Netherlands, according to a social survey, only 18% of shareholders expect a return on social investment of pension funds, most of them are interested in the social effect and positive chang-

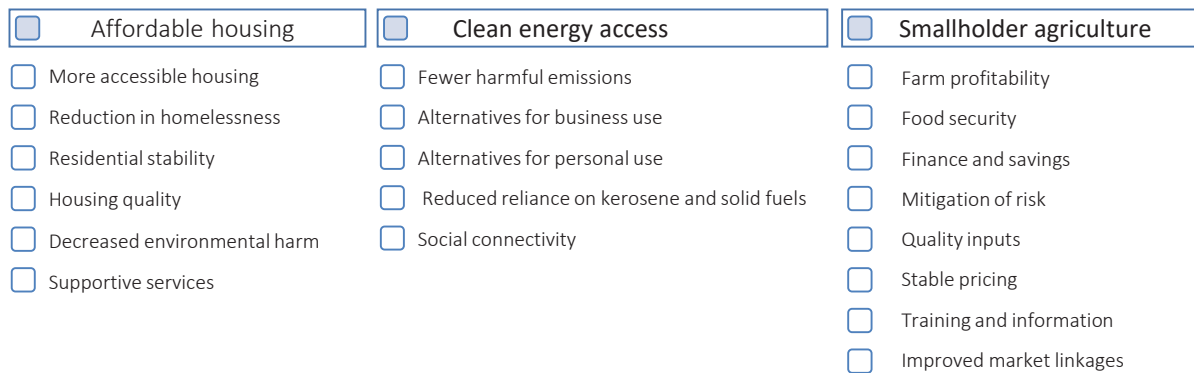


Figure 2. Perspective areas of impact investing in Ukraine

es in society and only then in gaining profit (Olginskij, 2017).

Impact investments are managed into social projects, companies, enterprises, organizations, NGOs, and funds with the intention to generate positive social or environmental impact, or both alongside a financial return.

Though, one of the core features of impact investing is its range of return expectations and asset classes, which varies from concessionary market to market rate investments.

Due to the developed ecosystem of impact investing, there is a considerable progress in various sectors of the economy in foreign countries. Olginskij (2017) cites the latest data, under which the main branches of social investment today are: affordable housing (24%), financial inclusion (14%), alternative energy access (13%), financial services (10%), agriculture (6%), health (3%), education (3%).

As for the growth rate of impact investing, the fastest are in agriculture, alternative energy, health care and education.

Promising future directions strategically conceived by the GIIN in the social investing sector are: the affordable housing in developed markets, smallholder agriculture in emerging markets and clean energy access in emerging markets.

Future investment themes may include: financial services, healthcare, gender and land conservation.

3. DISCUSSION

Taking into account the strategic needs of the country and in order to form and develop a qualitative impact investing ecosystem in Ukraine, it is expedient for the parties of the studied process to draw on the positive experience of foreign countries and to develop the following perspective areas of social investment (Figure 2).

Despite the fact that impact investing is quite comparable in yield to many classical financial instruments (as shown by objective financial analysis), most of the business community continues to view them as an instrument of political and social activity rather than commercial activity.

Another obstacle to the development of impact investment in Ukraine is that, unfortunately, the issue of cooperation between the business sector and the government, as well as within the society is, today, quite controversial, but in the field of social entrepreneurship, there is one common goal for all subjects of internal relations – making society's life more comfortable and leveling up social hardships and problems. Awareness of this fact will make it possible to move from the point of view of the creation of a favorable infrastructure for both social enterprises as a whole and social investment ecosystem in particular.

The development of the ecosystem of impact investment in the country plays a significant role in addressing a range of socio-economic and political tasks, namely:

- raising the welfare of the population;
- environmental protection;
- improvement of working conditions;
- improvement of the health system and demographic situation;
- progressive development of all sectors of the national economy;
- ensuring national security and military power of the state;
- strengthening the position of the state in the international arena;
- creating the image of the state as a worthy partner and an important subject of international relations.

Taking into account the fact that an important component of a quality ecosystem of impact investing in the country is the awareness of the need for competent training of the community and its leaders to address socially significant problems and to develop impact investments in Ukraine in general, it is necessary to note the existence of an

appropriate state structure – the Ukrainian Social Investment Fund (USIF).

USIF is a non-profit organization financed by donors with financial resources provided within the framework of projects of international technical assistance and projects of economic and social development of Ukraine supported by the World Bank and other international financial organizations.

One of the priority areas of UFSI’s activity is the development of the capacity of local communities, which is carried out through the continuous training of public leaders.

Thus, it can be argued that UFSI’s activities are aimed at the continuous development of the community and its members through community leaders representing the public interest.

In the process of such continuous development, community leaders acquire certain skills necessary to achieve a socially useful goal (Figure 3).

Such skills and their acquisition by the communities’ representatives in Ukraine is the necessary condition of development of impact investing ecosystem in the country.

Source: Own compilation.

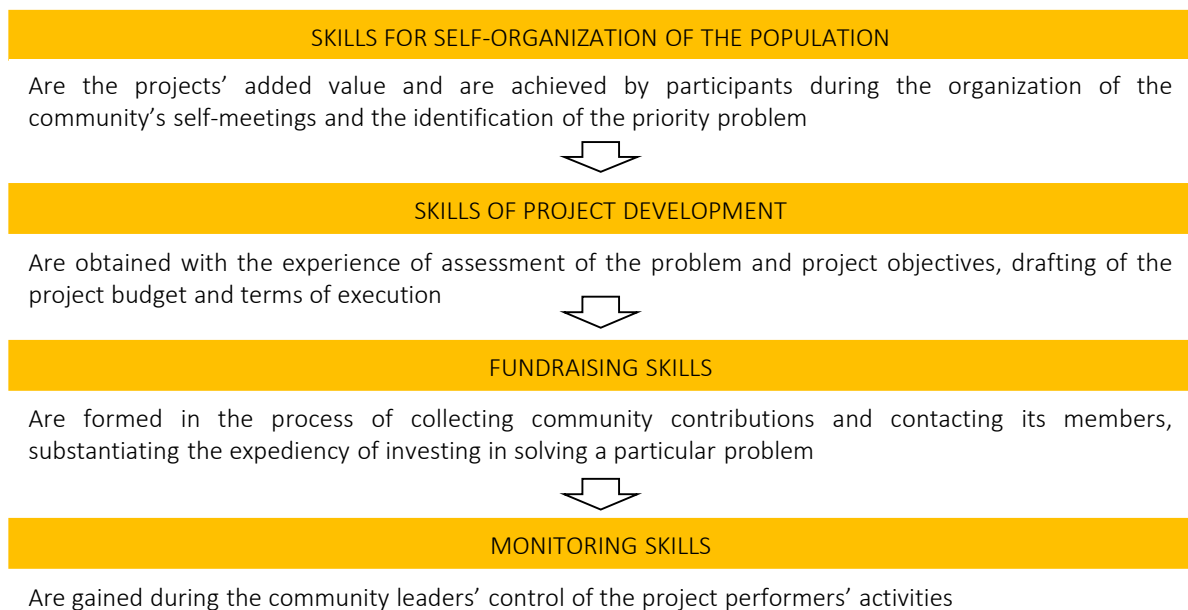


Figure 3. Methodology for acquiring impact investing skills

The specific nature of socially oriented entrepreneurship lies in the duality of its essence: on the one hand, the social enterprise acts as a mean of social impact on the process of social and political transformations to the same extent as on the state as a whole; on the other hand, it is a business solution to numerous social problems.

In one way or another, the state is directly interested in the social enterprise, which actually assumes a part of the functions and responsibilities of public authorities.

The experience of foreign countries has proved that social entrepreneurship is able to fulfill certain social and economic functions of the authorities, indeed, in certain circumstances, is even more effective mechanism for solving social problems than state power. The effectiveness of fruitful cooperation between the state and social enterprises is possible only if the fundamental guidelines are correctly identified. First and foremost, the purpose and principles of interaction, strategic priority areas and forms of mutually beneficial cooperation should be marked.

An urgent need in this regard is the adoption of the Law on Social Enterprises No. 10610 dated June 14, 2012 by the Parliament of Ukraine – The Verkhovna Rada, which will enable Ukraine to create an institutional basis for the functioning of social entrepreneurship.

Accordingly, the tasks of public administration in this context are the enforcement and development of an effective model of the relationship between the state and the socio-entrepreneurial sector with a view to provide support to it and to contribute to its development.

The analysis of the current state of the socio-entrepreneurial sector of the economy of different countries (including Ukraine) makes it possible to distinguish three main priority directions to implement public policies in the area of social entrepreneurship.

First, the main challenge at the current stage is to ensure a favorable institutional environment and appropriate infrastructure for social enterprises, which implies:

- adoption of the legislative framework;
- establishment of appropriate public agencies and institutions, implementing public policy on promoting and supporting social entrepreneurship;
- creation and development of financial infrastructure.

Second, a major step towards social entrepreneurship on the part of the state is the development of a public-private partnership institution involving socially-oriented enterprises to participate in trial competition for the performance of public procurements. This issue acquires particular relevance at the initial stage of social entrepreneurship in the country where the state often acts as social enterprises' only customer.

Thirdly, it is necessary to apply a systematic approach in complete and comprehensive solution to the question of competence of social entrepreneurs. Experience from different countries suggests that social entrepreneurs are more aware of social priority issues than the state. On the other hand, they do not always have a clear understanding of how to address these issues and to apply business skills. Accordingly, the function of the state in this context is to provide consultative and informational assistance to the social entrepreneurship sector as much as possible.

The ecosystem of impact investing in Ukraine is on the transitional stage. Its development depends, first of all, on overcoming certain socio-economic and legal barriers at an initial stage, namely:

- low level of public understanding about the very essence of impact investing. Accordingly, the lack of necessary level of trust and support from the community. It is with the purpose of raising the awareness of the citizens of the country about impact investing that the Ukrainian Social Investment Fund carries out its activities.
- lack of clear frameworks of impact investing in the country. The obstacle is a derivative from the previous one, because the lack of un-

derstanding of the essence of the concept of impact investing leads to discrepancies in its goals and motives within the social project or social program itself.

- absence of clear legal regulation and uncertainty of the “rules of the game” at the legislative level. On the other hand, the lack of strict legal regulation opens up broad opportunities for social investment in Ukraine, as state regulation causes additional economic costs and limits the flexibility of managers in the decision-making process. By engaging in impact investing, the company may expect a reduction in pressure from public authorities.
- openness and publicity of enterprises. Each social program must be clearly spelled out and presented to the public. This implies absolute openness and transparency in the process of impact investing, which, unfortunately, is not

a characteristic feature of the economic environment in the country today.

The main directions of the development of the ecosystem of impact investing in Ukraine today should be the traditional mechanisms of social security – pension and health insurance, employment and unemployment assistance, income indexation, benefits and payments to certain segments of the population, assistance to the poor, etc. (both from the state and on the part of employers in accordance with the law), as well as comparatively new directions, such as supporting the activities of specialized social investment institutions and the development of promising impact investing sectors: affordable housing, providing access to low-cost electricity and investments in clean energy sources – solar energy, wind and thermal energy, energy agriculture, the development and expanded use of renewable energy, etc.

CONCLUSION

Despite the fact that the concept of social investment or impact investing is rather new for Ukraine, it is necessary to note the high level of interest and engagement in it from both the public and potential and current investors. The development and implementation of social programs positively affects the formation of a good record in society, which, in the end, increases sales, provides the opportunity to hire skilled workers, access to public funding and other benefits.

The development of impact investing ecosystem in Ukraine will contribute to solving urgent socio-economic problems through diversification of the process of providing social services to the population, will create more opportunities for employment and self-employment, and will stimulate the processes of activation and consolidation of society.

Of course, there are certain impediments to the development of the impact investing ecosystem in Ukraine that are in the scope of the paper. In addition, the public’s request for a social investment institution is currently underdeveloped. Nevertheless, given the positive experience and results of foreign countries in this regard, where state support for impact investing and the creation of the appropriate infrastructure is a common practice, one can assert tremendous prospects of development of areas of social investment in Ukraine.

On the other hand, the theory and practice of state regulation still lack the conceptualized mechanisms of impact investing and the corresponding institutional environment – this situation is typical, in particular, for Ukraine.

Accordingly, the task of public administration in this context is to develop and implement in practice an effective model of relations between the state, private entrepreneurship and social sectors for their support and promotion, which provides a broad scientific basis for further study and establishment of mechanisms for the development of the impact investing ecosystem in Ukraine.

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