ADOPTING THE LONDON PRINCIPLES:

Policy Considerations to Grow Impact Investing in Hong Kong

Executive Summary • July 2014

Co-authors: Philo Alto and P. Ming Wong

Published By:

ASIA COMMUNITY VENTURES
同舟共濟

Supported By:

THE ROCKEFELLER FOUNDATION

In Partnership With:

IIPC
IMPACT INVESTING POLICY COLLABORATIVE

PREFACE

This paper seeks to provide action-oriented insights for policy makers and practitioners exploring the use of impact investing to address Hong Kong's most pressing social issues. Although our focus is Hong Kong, we believe many of our observations remain relevant for other cities considering the use of policy to grow impact investing.

Working on EngageHK[1], our 18-month mapping exercise of Hong Kong's social ecosystem, allowed us to engage with many of our city's leading practitioners in their respective fields. We studied seven sub-sectors – academia, corporations, foundations, intermediaries, non-profits, social enterprises and government. Collectively, we refer to these stakeholder groups as comprising Hong Kong's social ecosystem. Given its size, the Hong Kong government plays a significant role via its policies across departments, funding of social welfare services, either directly or through various subventions to non-profit organizations.

Although we have observed policy to be a critical factor in supporting Hong Kong's social ecosystem, a proper analysis of existing government policy was outside the scope of our original EngageHK mapping exercise. We have therefore written this follow-up report to expand on the role of government and to show how the development of impact investing globally presents an opportunity for governments to supplement traditional funding with impact investment capital in addressing pressing social issues.

Soon after we commenced work on this research, the Hong Kong government announced the launch of its HK$500 million (US$65 million) Social Innovation and Entrepreneurship Development Fund (SIE Fund). This unexpected but welcomed development presented us with an opportunity to reframe our approach to craft a more action-oriented report, along with specific suggested approaches, given the quickly evolving landscape in Hong Kong resulting from the launch of the SIE Fund.

The SIE Fund's primary objective of developing social innovation and entrepreneurship for poverty alleviation, coupled with its focus on supporting intermediary organizations, resonates strongly with the recently announced London Principles of Impact Investing. The Impact Investing Policy Collaborative developed this set of policy guidelines to assist governments that are considering impact investing as a tool to address social objectives.

By embracing these principles in its policy design and leveraging its position as a financial hub, Hong Kong is well placed to establish itself as an international hub for social innovation and impact investing for Mainland China and the rest of Asia. In doing so, Hong Kong has the opportunity to tap into fresh global resources and attract new talent pools to Hong Kong to build a better and more sustainable future for the city and the region.

P. Ming Wong and Philo Alto
Co-Founders, Asia Community Ventures

1 Asia Community Ventures, Mind the Gap: Lessons and Findings from EngageHK, August 2013. International readers who might be less familiar with Hong Kong are encouraged to read this EngageHK report, along with Section 2: Commission on Poverty and Hong Kong Poverty Situation, for additional background and history of the Hong Kong social space.

Cover photo credit: WMA Open Photo Contest 2012 – "Scavenger" by Palma Phey

EXECUTIVE SUMMARY

Hong Kong's five ongoing social funds as well as the new HK$500 million (US$65 million) Social Innovation and Entrepreneurship Development (SIE) Fund (see box in page 9) are well intentioned. However, until they begin to recognize and address longer-term social issues and embrace social innovation, including new tools like impact investing, they will unfortunately remain inadequate to address the root causes of poverty in Hong Kong.

These social funds provide important background on the development of the social sector in Hong Kong as well as lessons on what has worked and what has not. Our analyses of these social funds reveal the following three observations.

1. Different Approaches, One Shared Goal

Although every social fund has its own unique objectives in terms of target groups or issues (e.g. socially disadvantaged groups, food support), themes (social innovation, social capital, cross-sector collaboration), or strategies (immediate relief vs. long-term support), they share the same underlying goal, which is to help those who are trapped in poverty to springboard towards self-sufficiency. These social funds, however, remain largely disconnected and lack a coherent narrative to underscore how they contribute to the longer-term social well-being of Hong Kong.

2. Variations of Government Subventions

While claiming to support social enterprises, Hong Kong's social funds are, in practice, variations of conventional government subventions as they restrict the eligibility of applicants to not-for-profit organizations. The SIE Fund's willingness to embrace new ways of funding will foster collaboration across organizations towards a target social issue or group. It will also potentially enable social entrepreneurs to obtain funding support, through intermediaries, to unleash the potential of innovation to break the cycle of poverty.

3. Lack of Sustainability and Scalability

Relying solely on the public sector to solve Hong Kong's poverty issue is neither sustainable nor scalable. The Government should go beyond providing grant funding and catalyze private capital, networks and ideas for addressing social issues. Of all the funds we studied, the SIE Fund has the greatest potential to crowd-in resources from other players, including corporations and institutional investors, high net-worth investors and foundations, philanthropists and impact investors, thereby multiplying its impact.

We believe the SIE Fund offers the best prospect for enabling social innovation. For this to happen, care must be taken to ensure that it is properly designed and executed.

The five existing social funds will continue to play a valuable role. But the Government needs to share the successful outcomes generated by these funds. At the same time it should also acknowledge and learn from any shortcomings in these funds. The creation of these funds does not represent the final destination. Rather the funds form part of Hong Kong's journey towards greater sustainability and poverty alleviation. Therefore uses of these funds should be evaluated and adjusted where necessary to be responsive to evolving social needs.

We believe impact investing is an important tool in this journey. The key attractions of impact investing in tackling social and environmental problems include:

- engagement of the private sector
- attraction of fresh capital to complement government funding
- use of business approaches and impact measurement
- encouragement of new cross-sector talent and career paths
- deepening and expansion of growth capital to allow scaling (because grants are not always the appropriate tool)
- recycling of capital for future investments

The London Principles of Impact Investing provide a policy framework for governments to develop the impact investing market in collaboration with the other sectors in the social ecosystem. We now show below a summary of the London Principles, followed by how each principle might be applied in Hong Kong.

The London Principles of Impact Investing

Launched in July 2013 by the Impact Investing Policy Collaborative (IIPC), the *London Principles* for impact investing, in summarized form, are as follows:

1. *Clarity of purpose* – speaking to the importance of vision, leadership and perspective on what impact investing can realistically accomplish.
2. *Stakeholder engagement* – bringing design principles to surface ideas, engender public support, and ensure policy is well targeted to expressed needs.
3. *Market stewardship* – recognizing that policies that increase the supply of impact investing capital must balance those that strengthen social enterprises and other capital recipients, together with intermediary infrastructure.
4. *Institutional capacity* – providing for the appropriate expertise, resources, and durability within government to ensure successful policy implementation.
5. *Universal transparency* – locking in accountability and supporting a culture of continuous, open learning and improvement among all actors in impact investing.

The London Principles are

- intended to assist governments considering impact investing as a tool to address social objectives. They do not dictate what a government should do, but rather offer guideposts that ideally point to better strategy and policy development.
- drawn from a multitude of political, economic, and cultural contexts, and have been developed to address different places across varying stages of impact investing ecosystem development.
- designed to support a reflective approach to policy that drives learning and innovation over time to achieve important social objectives.

1. Clarity of Purpose

The Government has historically been taking a cautious role in policy making, often resulting in spending resources to tackle immediate symptoms instead of the root causes of social problems. Due to its positive non-interventionist mindset, the Government has yet to articulate a longer-term social vision to guide its policy formulation and appears to be driven, instead, by political expediency.

Our suggested approach for the Government:

a) create an impact investing agenda to address longer-term social challenges confronting Hong Kong, particularly economic inequality.

b) establish a separate Office of Social Innovation (OSI) with a steering group that includes the Efficiency Unit and Innovation and Technology Commission, among others. The OSI will have an expanded mandate to promote social innovation within Government and across sectors through its funding, regulating and convening powers.

c) conduct a holistic review of existing and new social funds. A needs based assessment should be required for all existing social funds prior to any decision of topping-up. We also recommend promoting shared learning, reducing overlap and bureaucratic red tape, and streamlining processes whenever possible.

2. Stakeholder Engagement

A key finding of EngageHK is a lack of cross-sector collaboration and knowledge sharing. In addition, there is an ingrained “siloed” mindset in the ecosystem, whereby for-profit and not-for-profit, including the Government, rarely collaborate beyond their traditional boundaries. Many of the social funds have been introduced in response to community interest groups’ clamors without the benefit of adequate cross-sector stakeholder engagement.

Our suggested approach for the Government:

a) provide a platform for people to express their views, and have a fair and transparent process on how to take these forward for policy review and setting.

b) use its power thoughtfully to fund, regulate, or incentivize other stakeholder groups in engaging them for its social funds whether as a fund recipient or an advisor in the nascent space of social innovation and impact investing.

c) engage with the global impact investing community, such as the International Social Impact Investment Taskforce, established by the G8 or the Global Learning Exchange

on Social Impact Investing convened by the UK Cabinet Office, Impact Investing Policy Collaborative (IIPC) and the World Economic Forum.

Our suggested approach for the SIE Fund:

d) reach out proactively to the media to explain the fund's objectives and how these are ultimately linked to addressing poverty and other issues in Hong Kong.

e) crowd-in additional resources and in-kind support from foundations and other private or corporate funds.

f) build on momentum from recent impact investing and social enterprise forums in Hong Kong to promote the city as an Asia hub for impact investing, social innovation and entrepreneurship.

g) feature exemplary individuals and organizations that contribute towards social innovations in their own ways or through cross-sector efforts or careers.

3. Market Stewardship

Broadly speaking, EngageHK findings identify the lack of an enabling environment and ambiguous definitions of social enterprises as key issues hindering the development of impact investing in Hong Kong. There is also a lack of awareness of the need for an intermediary sector to provide a platform for ideas exchange and capacity building in the social ecosystem. Policies that promote the development of both the demand and supply of capital to help the social sector grow are also needed.

Our suggested approach impacts on four key drivers, including:

a) On the **demand side**, partner with other players such as InvestHK to attract individuals and organizations with the most innovative ideas from around the world to establish their presence in Hong Kong and collaborate with local players. Leverage the SIE Fund to encourage social entrepreneurship, incubate and accelerate social enterprises as they scale.

b) On the **supply side**, fund research initiatives such as the feasibility of crowdfunding as an impact investing tool, devising policy ideas that encourage the private sector and foundations to fund more innovatively through tax and procurement incentives.

c) On **intermediary development**, leverage SIE Fund to support intermediaries across the spectrum of social incubators and accelerators as well as related service providers. Furthermore, resist temptation to spread out funding support in favor of providing targeted funding at scale.

d) On **policy and legal infrastructure (collectively, "ecosystem development"),** commission research through SIE Fund on the viability of hybrid legal structures, and pay for success programs to prepare the groundwork for impact investing.

4. Institutional Capacity

Social funds have been created to address specific community needs or social issues in relation to poverty alleviation. The ESR Fund, for example, which promotes the social enterprise approach to job creation for disadvantaged groups, is actually just another variation of social welfare funding. As a result of this rather outdated mandate, institutional capacity to foster social innovation is limited at best. In addition, the Government needs to measure and evaluate the impact of its own policies against stated objectives.

Our suggested approach for the Government:

a) review its departmental and policy focus to also be responsive to addressing structural social challenges in addition to immediate social welfare goals.

b) commission an internal review of existing institutional capacities and policies in addition to social funds to determine if they are in need of better implementation or a fresh re-think as informed by overseas experiences.

Our suggested approach for the SIE Fund:

c) appoint independent third parties to conduct performance reviews at the fund, intermediaries, and project levels.

d) release regular updates to allow all stakeholders to be fully aware of current developments to facilitate collaboration and generate learning opportunities.

5. Universal Transparency

While most EngageHK respondents recognize the benefits of transparency and accountability, which go hand in hand, there is a notable lack of perceived leadership on this front. The current political environment in Hong Kong is such that Government officials' wariness of media scrutiny hinders its ability to make bold, long-term decisions and consequently, affects its delivery of social remedies with long-term benefits.

Our suggested approach for the Government:

a) as a funder, promote competition for funding based on the merit of ideas and how well they address structural issues and not just immediate community needs.

b) as a regulator, foster trust and confidence by providing policy transparency and consistency in relation to impact investing.

c) as an enabler, support open data initiatives within and across sectors to facilitate cross-sector social innovation via technology.

Our suggested approach for the SIE Fund:

d) ensure that the SIE Fund is appropriately resourced with the relevant talent and infrastructure to provide fund and project management, governance and impact reporting.

e) allocate funding to support intermediaries and related service providers to develop tailored social impact measurement tools that fit the current Hong Kong context.

The London Principles exist to help governments from all over the world to design better policies to address social objectives. They are particularly relevant if the governments are looking to attract private capital to work alongside public resources to solve their most intractable problems.

The London Principles could serve as one of the key tools that would be useful to have in the policy toolbox for Hong Kong, even as it looks to leverage its financial hub status and is well placed to establish itself as an international social finance and innovation hub for Mainland China and the rest of Asia. In doing so, Hong Kong has the opportunity to tap into fresh global resources and attract new talent pools to build a better and more sustainable future for the city and the region.

Social Innovation and Entrepreneurship Development (SIE) Fund at a Glance

Objectives: To establish and support processes, schemes and experiments that attract, inspire and nurture social entrepreneurship to introduce and develop innovations that create social impact and build social capital to support poverty relief in Hong Kong.

Principles:

- Social innovation is the focus, not social enterprise per se;
- Scope of the Fund should remain flexible for more effective delivery of results based on actual experience;
- Focus on innovative ideas to alleviate and prevent poverty;
- Risk assessment is important while promoting innovation so as to maintain the prudent use of public money; and
- No overlap with other existing public funding.

Focus areas:

Funds will be distributed under the three priority areas – (1) research, (2) capacity building, and (3) innovative programs – through a variety of programs administered by intermediaries. It may also sponsor some theme-based flagship projects directly from time to time. In addition to the above, the Task Force will further deliberate various options including grant, matching grant and other types of funding.

Research

1. Undertaking or commissioning research to better identify areas of needs;

Capacity Building

2. Establishing or supporting schemes to reach into the community to spread awareness of social innovation and entrepreneurship, to encourage individuals to enter the field;
3. Establishing or supporting networks among bodies engaged in the field of social innovation and entrepreneurship to help build capacity and co-ordination across the field;
4. Establishing or supporting schemes to provide mentorship for aspiring social entrepreneurs;
5. Building networks that help connect aspiring social entrepreneurs with partners, finance or other support mechanisms;

Innovative Programs

6. Supporting existing mechanisms to provide seed or scale-up funding for innovative social entrepreneurs;
7. Establishing new funding mechanisms to support innovative social entrepreneurs that fill the gaps or complement existing programs; and
8. Funding suitable projects that meet the objectives of the Fund.

Hong Kong Social Sector – A Brief History

To better understand the context for policy review to grow impact investing in Hong Kong, we need to have a background understanding of the evolution of Hong Kong's social sector over the last sixty to seventy years.

Hong Kong's current social welfare policy can be traced back to its British colonial government's approach in addressing the socio-political issues facing Hong Kong from 1945 through the 1970s. The influx of refugees from Mainland China beginning with the communist revolution in the late 1940s has resulted in the development of large squatter camps throughout Hong Kong.

In the 1960s, the colonial government stepped up its social welfare provision efforts as civil society expectations grew for better working conditions, housing and health services. In 1974, the colonial government established the Independent Commission Against Corruption (ICAC) to address corruption and rebuild public confidence. Collectively, these initiatives laid the foundation for the colonial government's reputation in the 1970s onward as having a strong rule of law, and an efficient and corruption-free public administration. The economic boom in the 1970s and 1980s reinforced a minimalist approach towards social welfare.

In the early 1980s, the colonial government's priority was to cement its legacy through the continued expansion of the city's economy prior to China resuming sovereignty over Hong Kong in 1997. It built up the city as a pre-eminent financial hub in Asia on the foundation of a light-touch, low tax regime. As a result, outside of public social welfare support, the tax system minimized the burden on the rich, with limited incentives for social responsibility.

The post-1997 Government seemed to have inherited this aversion to social welfare funding beyond what was necessary. Government spending, through its various social funds, has evolved over time reflecting immediate responses to disparate community demands rather than a clearly articulated long-term vision for social services such as education, health, medical care, public housing, and social welfare.

In his January 2013 Policy Address, Chief Executive CY Leung announced the reinstatement of the Commission on Poverty (CoP) to more effectively support poverty alleviation policies. Its work included analyzing the poverty situation, setting up a poverty line, formulating new policies to prevent and alleviate both poverty and social exclusion, as well as promoting upward social mobility. This reinstatement of the CoP reflected a concern about the worsening plight of the working poor, as well as a lack of a rigorous benchmark upon which to define, measure and evaluate the success of government's policy efforts to address this issue.

ASIA COMMUNITY VENTURES | 同 舟 共 濟

Level 10, Central Building, 1-3 Pedder Street, Central, Hong Kong

Phone: +852 3478 7375 **Fax:** +852 3975 2800 www.asiacommunityventures.org