

Entrepreneurship Policy Research Division

### Policy Research

## Entrepreneurial Ecosystem Policy in Korea, 2013

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Government of the Republic of Korea; Small and Medium Business Administration; Financial Services Commission; Ministry of Strategy and Finance; Ministry of Science, ICT and Future Planning; Ministry of Justice; Ministry of Trade, Industry and Energy; Ministry of Employment and Labor; Ministry of Health and Welfare; Ministry of Government Legislation; Fair Trade Commission; Financial Supervisory Service; Korean Intellectual Property Office; Small and Medium Business Corporation; Korea Exchange

*Summary:* This report reviews the entrepreneurial ecosystem policy that the Government of the Republic of Korea set out from January to December 2013 in six domains — regulation and law, finance, culture, support, human capital and markets — and analyses it in its context, against theory and in practice. The government represented the problem as a blocked “virtuous circle” of start-up finance and promised investment instead of loans. Its designs, however, placed public money and guarantees at the centre and left the principal tax incentives, for angel investment and technology M&A, to pending legislation. Relief from failure was reserved for “honest failure”, and the other domains received many small programmes, reported as outputs rather than effects. Its best measures lowered the cost of failure, as the abolition of joint guarantees in non-bank lending did, or let private investors choose the firms that public money followed.

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# Entrepreneurial Ecosystem Policy in Korea, 2013

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# Entrepreneurial Ecosystem Policy in Korea, 2013

## Abstract

This report reviews and analyses the entrepreneurial ecosystem policy of the Government of the Republic of Korea as the government set it out in its own plans, reports and announcements: the work report of the Small and Medium Business Administration and the work plan of the Financial Services Commission, the joint plans of May, June and October, the Small and Medium Business Administration's report to the National Assembly, the Financial Services Commission's crowdfunding plan, the Ministry of Strategy and Finance's guide to the changes from 2014, and the announcements that implemented single measures. The policies are reviewed in six domains of the entrepreneurial ecosystem – regulation and law, finance, culture, support, human capital and markets – and analysed in their context, against theories of entrepreneurial ecosystems, entrepreneurial finance and business failure, and in practice. The government represented the problem as a blocked “virtuous circle” of start-up finance – loans instead of investment, missing exits and failure that ruins founders – and left markets, demand and the growth of the firms themselves largely outside the problem. Finance dominated the year: new funds and guarantees placed public money at the centre, and the principal tax incentives, for angel investment and technology mergers and acquisitions (M&A), depended on legislation still pending at the end of 2013. Relief from failure was reserved for “honest failure”. Programmes for education, incubation, ideas and public procurement were numerous but small and were reported in counts. The best-designed measures lowered the cost of failure or let private investors lead: the abolition of joint guarantees in non-bank lending, tax relief and shorter credit records for re-starters, and an incubator-linked programme in which private investors chose the teams that public research and development (R&D) money followed. Implementation was reported as funds formed, teams selected and a market opened; no plan or report set out how the effects of the main policies would be evaluated. The period covered is January to December 2013.

## Keywords

creative economy, start-up finance, angel investment, technology M&A, KONEX, crowdfunding, Growth Ladder Fund, second chance, honest failure, joint guarantees

## JEL Classification

L26, L53, M13, O38, H25

# 1 INTRODUCTION

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## Key findings

- The government represented the start-up problem as a blocked “virtuous circle” of finance: start-ups financed by loans rather than investment, too few exits for investors and failure that turns founders into credit delinquents. Markets, demand and the growth of the firms themselves were largely left outside the problem.
- Finance dominated the year. Public money from the Fund of Funds, the Korea Finance Corporation, the Korea Development Bank and the Industrial Bank of Korea anchored the new funds, the May plan provided for public money to take first losses in part of one fund, and new guarantees were added while the plans promised start-up finance through “investment, not loans”.
- Failure was reframed from a stigma into an asset to be recycled, but the October plan’s preferential re-start track and its debt relief for young founders were reserved for “honest failure”. The October plan blamed demanding requirements, among them strict moral-character evaluation, for the meagre reach of an earlier scheme; it proposed to consider waiving that evaluation, but only for those first classed as honest failures, and made “sound entrepreneurship” a condition of its guarantee waiver from 2014.
- The stage that was to close the circle, investors’ exit and reinvestment, opened with KONEX – a new stock market for small and medium-sized enterprises (SMEs) – and with eased merger rules and relief from gift tax for sellers, but its principal tax incentives, the larger angel deduction and the tax credit for technology M&A, depended on legislation that was still before the National Assembly at the end of 2013.
- The other domains received many programmes – entrepreneurship education from schools to universities, the Youth Start-up Academy, Creative Economy Town, a start-up visa and public procurement of new technology products – but most were small, and their progress was reported in counts of participants, teams and centres.
- The best-designed measures lowered the cost of failure or let private investors lead: joint guarantees were abolished in non-bank lending from July, tax relief and shorter credit records for re-starters took effect within the year, and in the incubator-linked programme experienced private investors chose the teams that public R&D money followed.
- Implementation was reported as outputs – funds formed, teams selected, a market opened – rather than effects, and no plan or report set out how the effects of the main start-up and finance policies would be evaluated, although their selection rules and eligibility thresholds would allow it.

The entrepreneurial ecosystem approach holds that new firms depend on many conditions at once – policy, finance, culture, supports, human capital and markets – and that governments go wrong when they act on only one or two of them (Isenberg, 2010, 2011). In 2013 the Government of the

Republic of Korea adopted this vocabulary: its plans spoke of building an “ecosystem” for the creative economy and a “virtuous circle” of start-up finance (Government of the Republic of Korea, 15 May 2013, 5 June 2013). This report reviews that policy as the government set it out in its own plans, reports and announcements, and examines it critically. It asks three questions:

1. What policies did the government set out in each domain of the entrepreneurial ecosystem in 2013?
2. How did the policies arise and how were they justified, how far were they valid in theory, and what had they achieved in practice by the end of the year?
3. What were their limitations, and what follows for policy?

The report draws on the policy studies and entrepreneurship literature where it bears on a policy – on problem definition and representation (Bacchi, 2009; Rochefort & Cobb, 1993), entrepreneurial ecosystems and clusters (Bresnahan, Gambardella, & Saxenian, 2001; Isenberg, 2011), entrepreneurial finance (Lerner, 2002; Riding, Madill, & Haines, 2007) and business failure (Lee, Peng, & Barney, 2007). The report is the first in an annual series on Korea’s entrepreneurial ecosystem policy.

Section 2 reviews the key policies of 2013 in six domains – regulation and law, finance, culture, support, human capital and markets – and assesses each. Section 3 analyses the policies in their context, against theory and in practice. Section 4 sets out the debates and contested points they raised and their theoretical limitations, and Section 5 their implications for policy.

The report rests on the plans, reports and announcements in which the Government of the Republic of Korea – chiefly the Small and Medium Business Administration (SMBA), the Financial Services Commission (FSC), the Ministry of Strategy and Finance (MOSF), the Ministry of Science, ICT and Future Planning (MSIP), the Ministry of Employment and Labor (MOEL) and the Ministry of Health and Welfare (MOHW), alone or in joint plans – set out its entrepreneurial ecosystem policy in 2013: plans adopted by the Cabinet or by the Ministerial Meeting on Economic Affairs, the SMBA’s work report and the FSC’s work plan, a report to the National Assembly, briefing materials, press releases and their annexes.

Table 1 lists the sources. The plans and reports set out or reviewed policy as a whole; the announcements introduced or reported a single measure. Quotations are IFED’s English translations of the Korean originals.

**Table 1: Government plans, reports and announcements reviewed**

| Subject                                                                               | Issuing bodies                                                                                                                                                                                                                              | Date and type                                                                          | Period covered         | Description                                                                                                                                                                                                              |
|---------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------|------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Plans and reports                                                                     |                                                                                                                                                                                                                                             |                                                                                        |                        |                                                                                                                                                                                                                          |
| 2013 work report                                                                      | Small and Medium Business Administration                                                                                                                                                                                                    | 25 March 2013<br>Annual work report                                                    | 2013                   | The SMBA's agenda for the creative economy, broken down into 97 detailed tasks: start-up and venture finance, entrepreneurship education, re-start support, sales channels and support for small business owners.        |
| 2013 work plan, with reference material                                               | Financial Services Commission                                                                                                                                                                                                               | 3 April 2013<br>Annual work plan and reference material                                | 2013                   | The FSC's agenda for the year, including a fund of funds for growth and exit finance, a special guarantee for prospective founders and a move away from lending based on collateral and guarantees.                      |
| Plan for a Virtuous Circle in the Venture and Start-up Financing Ecosystem            | Ministry of Strategy and Finance; Ministry of Science, ICT and Future Planning; Ministry of Justice; Ministry of Trade, Industry and Energy; Financial Services Commission; Fair Trade Commission; Small and Medium Business Administration | 15 May 2013<br>Joint plan, Ministerial Meeting on Economic Affairs, with press release | 2013                   | Measures to move start-up finance from loans to investment, centred on angel investment and M&A: tax incentives, KONEX, new public-private funds, guarantees and an incubator-linked programme for technology start-ups. |
| Creative Economy Action Plan: Measures to Build a Creative Economy Ecosystem          | Ministries and agencies jointly; the bodies named in its annex are listed in the note                                                                                                                                                       | 5 June 2013<br>Joint press release on the plan confirmed by the Cabinet on 4 June 2013 | 2013                   | The government's plan to build a creative economy ecosystem, presented as a break with the catch-up strategy; took up the May finance measures and added measures for ideas, people and first markets.                   |
| Plan to introduce crowdfunding                                                        | Financial Services Commission                                                                                                                                                                                                               | 26 September 2013<br>Press release with attached plan                                  | 2013                   | Proposal for investment crowdfunding through online intermediaries registered with the FSC, conditional on an amendment of the Financial Investment Services and Capital Markets Act.                                    |
| Status of work, report to the National Assembly for the audit of state administration | Small and Medium Business Administration                                                                                                                                                                                                    | 15 October 2013<br>Report to the National Assembly (audit of state administration)     | January–September 2013 | The SMBA's account of its work to September 2013 – funds, programmes, education, re-starts, public procurement and pending bills – with plans to 2014.                                                                   |

| Subject                                                         | Issuing bodies                                                                                                                                                                                                | Date and type                                                                              | Period covered  | Description                                                                                                                                                                                                    |
|-----------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------|-----------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Comprehensive Measures for SME Second Chances                   | Ministries jointly; responsible: Ministry of Strategy and Finance; Ministry of Science, ICT and Future Planning; Ministry of Justice; Financial Services Commission; Small and Medium Business Administration | 30 October 2013<br>Joint plan, Ministerial Meeting on Economic Affairs, with press release | 2013            | A “full-cycle” system from start-up to re-start: a staged waiver of founders’ joint guarantees, diagnosis-based restructuring, a fast rehabilitation procedure and support for re-starts after honest failure. |
| What changes from 2014                                          | Ministry of Strategy and Finance; the guide is issued in the name of the Government of the Republic of Korea                                                                                                  | 26 December 2013<br>Press release with summary and provisional edition of the annual guide | 2013            | Annual guide to the changes due from 2014, in a provisional edition.                                                                                                                                           |
| <b>Announcements</b>                                            |                                                                                                                                                                                                               |                                                                                            |                 |                                                                                                                                                                                                                |
| Minimum wage for 2013                                           | Ministry of Employment and Labor                                                                                                                                                                              | 1 August 2012<br>Press release with public notice                                          | 2013            | Minimum wage for 2013 set at KRW 4,860 an hour.                                                                                                                                                                |
| Duru Nuri social insurance subsidy at 50 % from April           | Ministry of Employment and Labor; Ministry of Health and Welfare                                                                                                                                              | 25 March 2013<br>Joint press release                                                       | From April 2013 | Social insurance subsidy for low-paid workers in workplaces with fewer than ten workers raised to a uniform 50 % from April.                                                                                   |
| Course-setting and rehabilitation consulting for SMEs in crisis | Small and Medium Business Administration; Small and Medium Business Corporation (SBC)                                                                                                                         | 18 April 2013<br>Press release                                                             | April 2013      | Course-setting and rehabilitation consulting offered for the first time to SMEs in management crisis.                                                                                                          |
| Kakao Youth Start-up Fund                                       | Small and Medium Business Administration                                                                                                                                                                      | 25 April 2013<br>Press release                                                             | April 2013      | Commitments signed for the first youth start-up fund sponsored by a successful venture firm, Kakao, for young founders and young firms.                                                                        |
| Abolition of joint guarantees in non-bank lending               | Financial Services Commission; Financial Supervisory Service (FSS)                                                                                                                                            | 26 April 2013<br>Press release with attached plan                                          | From July 2013  | Third-party joint guarantees abolished in non-bank lending for new contracts from 1 July 2013; existing guarantees to be removed within five years.                                                            |
| Opening of KONEX                                                | Financial Services Commission; Korea Exchange (KRX)                                                                                                                                                           | 29 June 2013<br>Press release with explanatory material                                    | July 2013       | Opening of KONEX on 1 July, a market for SMEs too small for KOSDAQ, with lighter listing and disclosure rules.                                                                                                 |
| Minimum wage for 2014                                           | Ministry of Employment and Labor                                                                                                                                                                              | 2 August 2013<br>Press release with public notice                                          | August 2013     | Minimum wage for 2014 set at KRW 5,210 an hour.                                                                                                                                                                |

| Subject                                                                 | Issuing bodies                                                                           | Date and type                                      | Period covered          | Description                                                                                                                                     |
|-------------------------------------------------------------------------|------------------------------------------------------------------------------------------|----------------------------------------------------|-------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------|
| Launch of the Growth Ladder Fund                                        | Financial Services Commission                                                            | 9 August 2013<br>Press release with annexes        | August 2013             | Launch of the Growth Ladder Fund, a fund of funds with KRW 1.85 trillion committed over three years, and its operating plan.                    |
| Launch of the Future Creation Fund                                      | Small and Medium Business Administration                                                 | 20 August 2013<br>Press release with attachment    | August 2013             | Formation of the Future Creation Fund at KRW 600 billion, above the KRW 500 billion planned, for start-ups and growth firms.                    |
| Laws taking effect from September 2013                                  | Ministry of Government Legislation (MOLEG)                                               | 27 August 2013<br>Press release with list of laws  | September 2013          | Laws taking effect in September 2013, among them deferred tax collection and tax relief for SME owners seeking to re-start.                     |
| Global start-up support programme launched                              | Ministry of Science, ICT and Future Planning                                             | 17 September 2013<br>Press release with annexes    | September–December 2013 | Launch of a programme of grants and mentoring for start-up teams aiming at global markets.                                                      |
| Creative Economy Town opens                                             | Ministry of Science, ICT and Future Planning; Korean Intellectual Property Office (KIPO) | 1 October 2013<br>Joint press release with annexes | From 30 September 2013  | Opening of Creative Economy Town, an online platform connecting citizens with ideas to mentors.                                                 |
| Technology start-up teams selected under the incubator-linked programme | Small and Medium Business Administration                                                 | 12 December 2013<br>Press release                  | May–December 2013       | Technology start-up teams selected by operators led by successful venture entrepreneurs, with government R&D matched to their angel investment. |
| KONEX at six months                                                     | Financial Services Commission; Korea Exchange                                            | 27 December 2013<br>Press release with report      | July–December 2013      | Review of KONEX's first six months: 45 listed firms against a target of 50, thin trading, and plans for the market.                             |

Source: The plans, reports and announcements listed. Periods covered and descriptions: IFEED.

Note: Where a plan or report has several parts, citations name the part (for example, plan or press release) before the page. The bodies named in the annex of the Creative Economy Action Plan are: Ministry of Strategy and Finance; Ministry of Science, ICT and Future Planning; Ministry of Education; Ministry of Foreign Affairs; Ministry of Justice; Ministry of National Defense; Ministry of Security and Public Administration; Ministry of Culture, Sports and Tourism; Ministry of Agriculture, Food and Rural Affairs; Ministry of Trade, Industry and Energy; Ministry of Health and Welfare; Ministry of Environment; Ministry of Employment and Labor; Ministry of Gender Equality and Family; Ministry of Land, Infrastructure and Transport; Ministry of Oceans and Fisheries; Office for Government Policy Coordination; Korea Communications Commission; Fair Trade Commission; Financial Services Commission; Anti-Corruption and Civil Rights Commission; Ministry of Food and Drug Safety; Korea Customs Service; Public Procurement Service; Defense Acquisition Program Administration; National Emergency Management Agency; Korea Forest Service; Small and Medium Business Administration; Korean Intellectual Property Office; Korea Meteorological Administration.

## 2 REVIEW OF ENTREPRENEURIAL ECOSYSTEM POLICIES IN KOREA

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This section reviews the key policies of 2013 in six domains, adapted from Isenberg's domains of the entrepreneurial ecosystem (Isenberg, 2011): regulation and law; finance, in grants, funding and financial infrastructure; culture; institutional support; human capital, in education and training and in labour; and markets, in market and industry support, initial public offerings (IPO) and exit. Each subsection describes a group of policies and assesses briefly whether it was a good policy; Section 3 analyses the policies as a whole.

### 2.1 REGULATION AND LAW

#### 2.1.1 JOINT GUARANTEES: ABOLITION IN NON-BANK LENDING AND A STAGED WAIVER FOR FOUNDERS

Joint guarantees by third parties, already abolished in bank lending, were abolished in non-bank lending – savings banks, mutual finance, specialised credit companies and insurers – for new contracts from 1 July 2013; for a corporate borrower one guarantee by its actual manager was still allowed, and existing guarantees were to be removed within five years (FSC & FSS, 26 April 2013, plan, pp. 5, 24; SMBA, 15 October 2013, p. 30). The October plan went further for founders themselves. It noted that the existing waivers had hardly been used because their thresholds were too high. It planned a staged waiver of the founder's own joint guarantee: within 2013 by lowering the rating threshold for the SBC's start-up loans, which on the loans made to September would have widened eligibility from 236 to 2,028 firms; from 2014 at the Korea Technology Finance Corporation, for start-ups with "excellent technology above a certain grade and sound entrepreneurship"; and more widely in a third stage, depending on the results and on "moral hazard" (Government of the Republic of Korea, 30 October 2013, plan, pp. 11–12).

The abolition was a good policy. It removed a liability that the May plan blamed for making recovery impossible for founders' families and employees after a single failure (Government of the Republic of Korea, 15 May 2013, plan, p. 13), and lowering the personal cost of failure can encourage entrepreneurs to pursue riskier, more promising opportunities (Lee et al., 2007). The waiver for founders was a mixed policy: beyond its first stage it was only announced, it was to run in three stages, and from 2014 it depended on a judgement of "sound entrepreneurship" whose criteria were to be worked out only by the end of 2013 (Government of the Republic of Korea, 30 October 2013, plan, p. 12).

#### 2.1.2 VENTURE CAPITAL AND START-UP REGULATION

The SMBA tightened the regulation of venture capital. To the existing sanctions for unfair practices by start-up investment companies – cancellation of registration and corrective orders – an amendment of the Support for SMEs Establishment Act in June 2013 added suspension of business, warnings, fines and penalties up to imprisonment, and a centre for reporting unfair practices was set up (SMBA, 25 March 2013, p. 46; SMBA, 15 October 2013, pp. 25–26). In September the Office of the Prime Minister and the SMBA announced deregulation for venture start-ups: the industries eligible for youth start-up funding were to be widened from January 2014 to include e-

commerce and tourism services, and those eligible for support under the Act by decree in the first half of 2014 (SMBA, 15 October 2013, pp. 23–24).

These were good but modest measures. Sanctions protect founders in their dealings with investors, and widening the eligible industries would remove rules that excluded new kinds of business. But the deregulation was set for 2014, and it widened the government's lists of eligible industries rather than replacing them.

### **2.1.3 REHABILITATION AND RE-START: TAX RELIEF, SHORTER CREDIT RECORDS AND A FAST PROCEDURE**

Several rules on failure changed. From September 2013 the Restriction of Special Taxation Act allowed the collection of tax arrears from SME owners seeking to re-start to be deferred and paid in instalments, and halved their income and corporate taxes for five years after a re-start (MOLEG, 27 August 2013, p. 2); the relief was limited to owners who had received the SBC's re-start loans, guarantees after review by the Credit Counseling and Recovery Service, or debt adjustment from that Service (SMBA, 15 October 2013, p. 31). In August the FSC shortened the period for which public credit records restrict the finance of rehabilitated firms, from five years after the event to three years after the court's approval of rehabilitation, on request and after review by the creditor institutions (SMBA, 15 October 2013, p. 31). The October plan proposed a fast rehabilitation procedure for SMEs, to be created by special provisions in law, which it expected to cut the time from the opening of proceedings to the approval of a rehabilitation plan from 8.6 months to 3.3–4 months (Government of the Republic of Korea, 30 October 2013, plan, pp. 20–21), and the SMBA and the SBC offered course-setting and rehabilitation consulting to SMEs in crisis for the first time (SMBA & SBC, 18 April 2013).

These were good policies. They went to the right target, the cost of failure, and the tax relief and the shorter credit records took effect within the year. But their reach was narrow: the tax relief went only to owners who had first passed a lender's or the Service's review, and the fast procedure was a proposal that needed legislation.

## **2.2 FINANCE: GRANTS, FUNDING AND FINANCIAL INFRASTRUCTURE**

### **2.2.1 GRANTS: GOVERNMENT R&D MATCHED TO ANGEL INVESTMENT AND START-UP COMMERCIALISATION**

In May the SMBA introduced an Israeli-style programme of start-up commercialisation R&D for global markets (the incubator-linked programme), in which operators led by successful venture entrepreneurs incubate and invest in technology teams and the government matches their angel investment with R&D funding (SMBA, 15 October 2013, p. 22; SMBA, 12 December 2013, pp. 1–2). Five operator consortia were selected in June and 15 teams by December, with KRW 6.35 billion of angel investment and government R&D in the first tranche, against 40 projects planned for 2013 (Government of the Republic of Korea, 15 May 2013, plan, p. 39; SMBA, 12 December 2013, p. 2). A customised start-up commercialisation programme, in which prospective founders choose the support that suits them, had supported 870 teams by September (SMBA, 15 October 2013, p. 21).

The incubator-linked programme was a good policy, the best-designed finance measure of the year: experienced private investors chose the teams and public money followed private money, as theory on public venture capital recommends (Lerner, 2002), although the plan set the public share at 85 % of each project's funding (Government of the Republic of Korea, 15 May 2013, plan, p. 39). Its weakness was scale — 15 teams against 40 projects planned — and the customised programme was reported only as a count of teams.

## 2.2.2 FUNDING: PUBLIC-PRIVATE FUNDS AND THE ANGEL INVESTMENT DEDUCTION

The SMBA formed the Future Creation Fund with large companies and other investors in August at KRW 600 billion, above the KRW 500 billion planned, raised “in only about 2.5 months” (Government of the Republic of Korea, 15 May 2013, plan, p. 22; SMBA, 20 August 2013, p. 1; SMBA, 15 October 2013, p. 25). The FSC launched the Growth Ladder Fund, a fund of funds for the flow of money from start-up to growth and exit, with KRW 1.85 trillion committed over three years by the Korea Finance Corporation, the Korea Development Bank, the Industrial Bank of Korea and the Banks' Foundation for Young Entrepreneurs (FSC, 9 August 2013, pp. 1, 3). Youth start-up funds sponsored by successful venture firms — Kakao and Smilegate, KRW 30 billion each — were formed in July and September (SMBA, 15 October 2013, p. 25). For private investors, a bill introduced in June would raise the income deduction for angel investment to 50 % of investments up to KRW 50 million and its ceiling to 50 % of income, and extend it to start-ups under three years old that had passed a technology assessment; registered angel investors rose from 2,608 in 2012 to 4,320 by September 2013 (SMBA, 15 October 2013, p. 26).

The funds mobilised money quickly, but they were a mixed policy. They rested on public anchoring: in the May plan, up to 60 % of each youth start-up fund was to come from the Fund of Funds, and the Future Creation Fund's early-stage account offered a priority return for private investors and a public first-loss account capped at KRW 20 billion (Government of the Republic of Korea, 15 May 2013, plan, pp. 23, 35). The same plan counted everything the new funds were expected to invest — 80 % of their size — as “additional investment”, part of KRW 4.3 trillion over five years, without estimating how much of that money would have been invested anyway (Government of the Republic of Korea, 15 May 2013, plan, p. 53), although tax-subsidised, government-sponsored funds can crowd out private venture capital (Cumming & MacIntosh, 2006). The angel deduction, the measure aimed most directly at private investors, was still a bill in October (SMBA, 15 October 2013, p. 26), and the tax amendments were still before the National Assembly at the end of the year (MOSF, 26 December 2013, press release, p. 2).

## 2.2.3 FINANCIAL INFRASTRUCTURE: GUARANTEES, RE-START LOANS AND CROWDFUNDING

The May plan added guarantees: a special guarantee for prospective founders from the Korea Technology Finance Corporation, a 100 % guarantee commitment of KRW 50 billion in 2013, and a guarantee of KRW 100 billion from the Korea Credit Guarantee Fund for the bank loans that acquirers take on (Government of the Republic of Korea, 15 May 2013, plan, pp. 23, 29). The special guarantee had been scheduled for March 2013 (FSC, 3 April 2013, reference material, p. 18), but none of the later plans and reports recorded its introduction. For failed founders, the SMBA

doubled the re-start loans from KRW 20 billion to KRW 40 billion in 2013 and offered young founders KRW 50 billion of start-up loans whose repayment could be adjusted after “sincere and honest” failure, by up to 40 % as a rule and up to 100 % at most (SMBA, 25 March 2013, p. 54); the October plan expanded these young founders’ loans to KRW 80 billion (Government of the Republic of Korea, 30 October 2013, plan, p. 13). The FSC’s crowdfunding plan of September proposed a channel of online intermediaries registered with the FSC through which many small investors could buy start-ups’ securities, available “from next year at the earliest” if the Financial Investment Services and Capital Markets Act was amended (FSC, 26 September 2013, pp. 2, 12).

The new guarantees were the weakest part of the finance policy and, as start-up policy, a poor one. The government promised start-ups financed by “investment, not loans” (Government of the Republic of Korea, 5 June 2013, p. 5), and the FSC itself diagnosed a financial sector that relied “excessively on collateral and government guarantees” (FSC, 3 April 2013, work plan, p. 7), yet the plans added guarantees without estimating how much of the guaranteed lending would not otherwise have been made, the test by which a guarantee is justified (Riding et al., 2007). The loans for failed and young founders were a mixed policy: they lowered the cost of failure, but the debt relief on the young founders’ loans depended on a finding of “sincere and honest” failure. Crowdfunding was a good policy in design, but at the end of the year it was still a plan.

## **2.3 CULTURE**

### **2.3.1 ENTREPRENEURSHIP: LECTURES, MENTORING AND START-UP AUDITIONS**

The SMBA set out to spread entrepreneurship with lectures by successful venture entrepreneurs and a nationwide tour of youth start-up forums, aiming at 1,250 events with 126,000 participants in 2013, and with camps and a contest (SMBA, 25 March 2013, p. 42); by September it reported 691 lectures by successful venture CEOs and young CEOs, attended by 92,547 people (SMBA, 15 October 2013, p. 22). The Creative Economy Action Plan had successful venture entrepreneurs visit schools to tell their stories and mentor pupils one to one (Government of the Republic of Korea, 5 June 2013, pp. 17–18), and the SMBA planned for December national start-up auditions such as the Practical Start-up League–Superstar V, whose league had selected six of 1,096 teams (SMBA, 15 October 2013, p. 24).

These were good measures for the culture domain, in which Isenberg places success stories and social norms (Isenberg, 2011), and they reached many people. But they were events counted by attendance, and they presented entrepreneurship mainly through the stories of those who had succeeded.

### **2.3.2 TOLERANCE OF FAILURE: RE-START CAMPAIGNS AND “HONEST FAILURE”**

The government also set out to change attitudes to failure. A Re-challenge SME Association was licensed in March 2013 to lead a campaign for a better environment for re-starts, and a conference on re-starts was planned for October (SMBA, 25 March 2013, pp. 54–55). The October plan, which observed that failed entrepreneurs were “branded as economic offenders and social dropouts” (Government of the Republic of Korea, 30 October 2013, plan, p. 8), added a televised audition in

which 50 re-starters would be trained and mentored and about ten finally supported, and an international conference on failure modelled on Silicon Valley's FailCon (Government of the Republic of Korea, 30 October 2013, plan, pp. 29–30). Preferential relief, however, was reserved for “honest failure”: the October plan limited its fast track for re-starters and its debt relief for young founders to those who had failed honestly, and left the details to a study to be commissioned at the end of 2013 (Government of the Republic of Korea, 30 October 2013, plan, pp. 12, 25–26).

The campaigns were a good policy: they addressed stigma directly, and stigma can weaken the encouragement that a forgiving treatment of failure gives to entrepreneurship (Lee et al., 2007). The test of honest failure was a poor one. It had a legitimate aim, to keep relief from rewarding the “moral hazard” that the October plan feared (Government of the Republic of Korea, 30 October 2013, plan, p. 12), but it worked against the campaigns. Failure is made sense of by attributing it to misfortune or to the entrepreneur's mistakes (Cardon, Stevens, & Potter, 2011), and by adding to that attribution a moral judgement of honesty and making it the gate to relief, the policy gave stigma an administrative basis — after an earlier scheme for failed venture entrepreneurs had reached only four people in seven years because of “demanding requirements such as strict moral-character evaluation” (Government of the Republic of Korea, 30 October 2013, plan, p. 7).

## **2.4 SUPPORT: INSTITUTIONAL SUPPORT**

### **2.4.1 INCUBATION: THE YOUTH START-UP ACADEMY, PROTOTYPE WORKSHOPS AND ONE-PERSON CREATIVE ENTERPRISES**

The SMBA expanded its residential incubator for young founders, the Youth Start-up Academy, from one site to four, for 300 founders, and its prototype workshops from one to four, which had produced 400 prototypes, designs and drawings by September (SMBA, 15 October 2013, p. 21). From March it ran seven leading start-up universities on the academy model, with dedicated space and coaching (SMBA, 15 October 2013, p. 22). For one-person creative enterprises it added broadcasting and other knowledge services to the eligible activities in September, raised the number of business centres from 34 in 2012 to 46 in 2013 and supported the marketing of 376 firms (SMBA, 15 October 2013, p. 23).

These were good policies of their kind: they supplied space, equipment and coaching, the supports on which new firms draw in Isenberg's model (Isenberg, 2011). Their scale was small beside the finance measures, and they were reported by the number of sites, founders and items made rather than by what became of the firms.

### **2.4.2 IDEAS: CREATIVE ECONOMY TOWN AND THE UNLIMITED IMAGINATION PROJECT**

The Creative Economy Action Plan promised that “any citizen with an idea becomes a protagonist” (Government of the Republic of Korea, 5 June 2013, p. 29). Creative Economy Town, an online platform built by the MSIP, KIPO and the Korea Institute of Science and Technology Information, opened on 30 September to connect people with ideas to mentors and to guide them from an idea to rights, finance, a prototype and marketing (MSIP & KIPO, 1 October 2013). The SMBA's Unlimited Imagination National Start-up Project (the idea project), launched in July, used crowd-sourcing to

select ideas: by September 5,357 ideas had been registered, 43 selected for commercialisation, 11 made into prototypes and six put into production (SMBA, 15 October 2013, p. 21).

This was a mixed policy. Opening policy to citizens' ideas was a reasonable aim, and the idea project met its plan for the pilot year, selecting 43 ideas for commercialisation against the 30 to 40 planned (Government of the Republic of Korea, 15 May 2013, plan, p. 38; SMBA, 15 October 2013, p. 21). Three months after launch it was too early for results, but the funnel — six products in production from 5,357 ideas — already suggested that ideas were plentiful and that what was scarce was the capacity to turn them into products and sales. The policy presumed that a good idea, once connected to mentors, rights and finance, would become a firm, a presupposition examined in Section 3.1.

### **2.4.3 GLOBAL START-UPS: THE GLOBAL START-UP PROGRAMME AND OVERSEAS SUPPORT**

The MSIP launched on 16 September a global start-up programme that, following its plan of 9 July, supported 20 start-up teams aiming at global markets from the start, together with three accelerators and two education bodies (MSIP, 17 September 2013). The SMBA supported 28 teams in starting up or expanding in three countries and opened a Korea venture investment centre in Silicon Valley in August to attract foreign capital and support Korean founders abroad (SMBA, 15 October 2013, pp. 23, 25).

Supporting firms that aim at foreign markets from the outset was a good policy for a small domestic market. The programmes were small, however — 20 and 28 teams — and two ministries ran them separately.

## **2.5 HUMAN CAPITAL: EDUCATION AND TRAINING, AND LABOUR**

### **2.5.1 ENTREPRENEURSHIP EDUCATION FROM SCHOOLS TO UNIVERSITIES**

The SMBA offered entrepreneurship education by age group. Bizcool, a business course in schools, ran in 135 schools in 2013; 30 universities ran 250 start-up courses and 300 start-up clubs; and 15 institutions ran practical start-up programmes for adults, with 524 participants by August (SMBA, 15 October 2013, p. 22). In September the Ministry of Education and the SMBA adopted a five-year plan for start-up education in universities, with start-up leave of up to two years, more special admissions for founders, disclosure of start-up activities in university information and the selection of universities with strong start-up capacity (SMBA, 15 October 2013, pp. 21–22), and dedicated start-up support organisations in universities were given a legal basis in June (SMBA, 15 October 2013, p. 22). The Creative Economy Action Plan set out to raise the number of university start-up education centres from 61 in 2013 to 100 in 2014 (Government of the Republic of Korea, 5 June 2013, p. 36).

This was a good policy, among the better ones of the year. Education builds some of the skills that research finds at the start of new entrepreneurial regions, although the firm-building capabilities it identifies come chiefly from experience (Bresnahan et al., 2001), and the five-year plan changed

university rules rather than adding another programme. Like the rest, however, it was measured by the number of schools, courses and participants.

### **2.5.2 FOREIGN FOUNDERS: THE START-UP VISA**

The May plan announced a start-up visa for foreign graduates with intellectual property (Government of the Republic of Korea, 15 May 2013, plan, p. 44). The plan of May 2013 to promote technology start-ups by foreigners and overseas Koreans, adopted by the Foreigner Policy Committee, set the visa for October, together with a programme of up to KRW 50 million to support foreign technology start-ups (SMBA, 15 October 2013, p. 23).

Opening the door to foreign founders was a good policy in principle. It addressed a small group, however, and the SMBA's report gave no target for the number of founders it was meant to attract.

### **2.5.3 LABOUR: THE MINIMUM WAGE AND THE DURU NURI SUBSIDY**

Labour policy was not presented as start-up policy, but it set costs that every small employer faces. The minimum wage for 2013, set by the MOEL in August 2012, rose by 6.1 % to KRW 4,860 an hour (MOEL, 1 August 2012, p. 7), and the rate for 2014 was set at KRW 5,210 in August 2013 (MOEL, 2 August 2013). At the same time the MOEL and the MOHW raised the Duru Nuri subsidy of social insurance contributions for low-paid workers in workplaces with fewer than ten workers to a uniform 50 % from April 2013 (MOEL & MOHW, 25 March 2013).

Each measure was sound on its own terms, and the subsidy offset part of the cost that the minimum wage raised for the smallest employers. As start-up policy, however, the result was poor by omission: none of the start-up plans and reports reviewed here – the SMBA's work report, the FSC's work plan, the joint plans and the report to the National Assembly – mentioned either, so the labour costs that every new employer faces were left outside start-up policy.

## **2.6 MARKET: MARKET AND INDUSTRY SUPPORT, IPO AND EXIT**

### **2.6.1 MARKET AND INDUSTRY SUPPORT: PUBLIC PROCUREMENT AS "FIRST CUSTOMER"**

The Creative Economy Action Plan acknowledged that ventures and SMEs with good products often struggle to open their first markets, and proposed that government and public institutions become their "first customer", through the selection of excellent procurement products and the public online shopping mall (Government of the Republic of Korea, 5 June 2013, pp. 6–7). The SMBA introduced in May priority purchasing from small firms for general items below KRW 230 million, prepared in August a plan to promote public purchasing of new technology products, and made the purchase ratio for products of women-owned businesses mandatory for public institutions from January 2014 (SMBA, 15 October 2013, p. 63).

Public demand addressed the domain that the finance plans neglected, and in direction this was a good policy. But the SMBA set it out in the part of its report on SMEs' sales channels, apart from its start-up agenda (SMBA, 15 October 2013, p. 15), and the measures were aimed at SMEs in general rather than at new firms.

### 2.6.2 IPO: KONEX

KONEX, a stock market for SMEs too small for KOSDAQ, with lighter listing and disclosure rules and direct trading limited to venture capital, institutional investors and individuals with deposits of at least KRW 300 million, opened on 1 July (FSC & KRX, 29 June 2013, explanatory material, p. 6; Government of the Republic of Korea, 15 May 2013, press release, p. 14); the FSC gave it the purpose of helping SMEs raise capital and move on to KOSDAQ (FSC & KRX, 29 June 2013, explanatory material, pp. 4–5). After six months it had 45 listed firms against 21 at opening, short of the 50 targeted, and trading was thin (FSC & KRX, 27 December 2013, report, pp. 5, 9–10).

KONEX opened on time and gave young firms an earlier route to public equity, which made it a good policy. Its first results were modest, and as part of the circle of finance it served investors' exits rather than firms' markets.

### 2.6.3 EXIT: TECHNOLOGY M&A

For exit through M&A, a bill of July 2013 proposed a corporate tax credit of 10 % of the technology value acquired in a technology-innovative M&A; a decree of September exempted the shareholders of sellers in arm's-length M&A from gift tax; a decree notified in October would defer for three years the inclusion of an acquired venture or R&D-intensive SME among a large acquirer's affiliates; and an amendment of the Act on Special Measures for the Promotion of Venture Businesses in June eased the requirements for small-scale and simplified mergers (SMBA, 15 October 2013, p. 27). The government's year-end guide listed the M&A tax credit as a new measure effective from 1 January 2014, "provisional, amendment under deliberation in the National Assembly" (MOSF, 26 December 2013, guide, p. 57).

The policy was mixed. The relief from gift tax and the easier mergers took effect and the deferral of affiliate status reached a draft decree, but the main incentive still awaited legislation, and the May plan's guarantee for acquirers' bank loans sat uneasily with its own diagnosis that reliance on borrowing burdened M&A (Government of the Republic of Korea, 15 May 2013, plan, pp. 11, 29).

### 3 ANALYSIS OF THE POLICIES

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#### 3.1 CONTEXTUAL ANALYSIS: ORIGINS, BACKGROUND AND RATIONALE OF THE POLICIES

The policies of 2013 were the first of a new government, which made the “creative economy” the organising theme of start-up and SME policy. The Creative Economy Action Plan, confirmed by the Cabinet on 4 June, presented the new policy as a break with “the catch-up strategy that led our economy’s growth over the past forty-odd years”, which, it said, had “hit its limits” (Government of the Republic of Korea, 5 June 2013, pp. 1–2), and the SMBA titled its work report “realising an era of the creative economy in which SMEs grow and small business owners are happy” (SMBA, 25 March 2013, p. 1). Policy was organised as national agenda tasks, which the SMBA broke down into 97 detailed tasks (SMBA, 25 March 2013, p. 19). The plans followed one another: the SMBA’s work report of March and the FSC’s work plan of April set out the agenda (FSC, 3 April 2013; SMBA, 25 March 2013); the May plan, announced by seven ministries and agencies at the Ministerial Meeting on Economic Affairs, disclosed “in advance the key contents of the venture and start-up part” of the wider plan (Government of the Republic of Korea, 15 May 2013, press release, p. 2); the Creative Economy Action Plan took these measures up (Government of the Republic of Korea, 5 June 2013); and the crowdfunding plan of September and the October plan added two further lines (FSC, 26 September 2013; Government of the Republic of Korea, 30 October 2013).

The government’s account of the background pointed two ways. New incorporations had risen — from 36,081 in the first eight months of 2008 to 51,057 in the same months of 2012 — but were flat in 2013, at 51,151, and the SMBA wanted to sustain what it called a recent climate of start-ups (SMBA, 15 October 2013, p. 20). At the same time nearly one start-up in two — 45 % in the SMBA’s own survey cited in the October plan — closed within three years (Government of the Republic of Korea, 30 October 2013, plan, p. 5), and the October plan set out to complete a “virtuous-circle business ecosystem” by drawing able people into start-ups and helping the firms to survive and grow (Government of the Republic of Korea, 30 October 2013, plan, p. 4).

Read through Bacchi’s first question — what the problem is represented to be (Bacchi, 2009) — the plans of 2013 represented the problem of entrepreneurship in one dominant way: as a blockage in the circulation of money. The May plan presented the venture funding ecosystem as one part of the creative economy ecosystem and left the path from idea to start-up to separate measures (Government of the Republic of Korea, 15 May 2013, plan, p. 4), but within that scope it located the deficit in private investors’ incentives and in exit institutions. Early-stage firms, it said, depend on loans mainly because “people who have succeeded once”, and so “people who really know”, do not invest (Government of the Republic of Korea, 15 May 2013, press release, p. 5); and investors hesitate, and successful founders cannot reinvest, because no channel other than a KOSDAQ listing exists for recovering venture money early (Government of the Republic of Korea, 15 May 2013, plan, p. 4; Government of the Republic of Korea, 15 May 2013, press release, p. 9). The SMBA and the FSC framed the problem in the same terms — “loan-oriented financing, an inadequate intermediate exit market (M&A) and an environment in which recovery is difficult” (SMBA, 25 March

2013, p. 39), and lending that relies on collateral and guarantees (FSC, 3 April 2013, work plan, pp. 7, 21). In the terms of Rochefort and Cobb (1993), the government defined the problem by its cause – the structure of finance – and by a population of founders without investment rather than firms without customers, and the definition already contained its solution: the May plan’s diagnosis and its remedy share one vocabulary of loans, investment and exits (Government of the Republic of Korea, 15 May 2013, plan, pp. 4, 15).

These representations rest on presuppositions that the plans argued little or not at all. The first is that money, not the quality of ideas or the demand for products, is the binding constraint: the Creative Economy Action Plan promised that “anyone with just a good idea can easily start a business” (Government of the Republic of Korea, 5 June 2013, p. 5). The second is that start-ups create jobs and that more of them are therefore good in themselves: the SMBA wrote that start-ups “create most jobs in Korea, the United States and elsewhere” (SMBA, 25 March 2013, p. 38), supported by gross figures of the jobs that new firms create (SMBA, 25 March 2013, p. 39). The third is that the benchmark lies abroad: the May plan set out to rebuild the domestic venture ecosystem “into a shape that rivals Silicon Valley” (Government of the Republic of Korea, 15 May 2013, press release, p. 2), and the crowdfunding plan cited moves to institutionalise crowdfunding in the United States, Italy, the United Kingdom and Japan as its warrant (FSC, 26 September 2013, p. 7).

What these representations left unsaid matters as much. Markets – the customers, demand and sales channels of new firms – entered the core plans only at the margins of the start-up problem: the Creative Economy Action Plan proposed that the state act as a “first customer”, and the SMBA set out its measures for SMEs’ sales channels apart from its start-up agenda (Government of the Republic of Korea, 5 June 2013, pp. 6–7; SMBA, 25 March 2013, pp. 83–85). The plans placed the first risk on public money but did not say what it might cost: the May plan provided for a first-loss account of public money of up to KRW 20 billion and, as a rule, a priority return for private investors (Government of the Republic of Korea, 15 May 2013, plan, p. 23), and the FSC planned funds in which policy finance “bears more of the investment risk” (FSC, 3 April 2013, work plan, p. 32), but none estimated the expected losses. And the plans described the distribution of their benefits only in passing: the May plan illustrated the angel deduction with an investor who puts KRW 50 million a year into a venture and pays income tax at 38 %, without asking who could invest on that scale (Government of the Republic of Korea, 15 May 2013, press release, p. 7).

The rationale of the policies was therefore only partly sound. The financing gap that the government described had a basis in its own figures, which showed angel investment falling from KRW 97.1 billion in 2006 to KRW 13.8 billion in 2012 (FSC, 26 September 2013, p. 6), and the personal cost of failure was a reasonable target. Theory gave the gap a weaker warrant than the plans assumed: credit rationing explains why lenders hold back from young firms whose risk they cannot observe (Stiglitz & Weiss, 1981), but the plans located the gap in equity rather than in credit, with 99 % of SMEs’ finance already coming from loans (Government of the Republic of Korea, 15 May 2013, plan, p. 8). But the rationale was narrow: it presumed that money, rather than skills, ideas that can be sold or demand, was the binding constraint, and it measured Korea against a foreign

benchmark rather than against the conditions of Korean firms. Table 2 summarises the representation in each of the main plans and reports.

**Table 2: How the SMBA, the FSC and the joint government plans represented the problem**

| Plan or report                             | Problem represented                                                                                                   | Presupposition                                                                                                                  | Left unsaid                                                                                                                                                                                         |
|--------------------------------------------|-----------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| SMBA work report (25 March 2013)           | An incomplete circle: ideas do not become firms because finance runs on loans, exits are rare and failure is punished | Start-ups are the main source of jobs; the state can build the ecosystem                                                        | Losses on new public funds; criteria for “honest” failure; investor protection in crowdfunding                                                                                                      |
| FSC work plan (3 April 2013)               | Lending based on collateral and guarantees, missing risk capital and missing exits                                    | Finance is the lever that creates jobs; the Korea Technology Finance Corporation can value technology for lenders and investors | Who absorbs losses when policy finance bears more risk; size and sources of the new funds                                                                                                           |
| Plan for a Virtuous Circle (15 May 2013)   | Blocked circulation of money because successful people do not invest and cannot exit early                            | Liquidity is plentiful; successful founders are the right investors; Silicon Valley is the yardstick                            | Downside risk of the public first-loss account and of guarantees; distribution of tax benefits; basis of the parameters behind the projected effects, including full additionality of the new funds |
| Creative Economy Action Plan (5 June 2013) | An exhausted catch-up model and an ecosystem in which ideas do not turn into start-ups                                | A good idea suffices to start a business once finance is available; ventures and SMEs create more jobs                          | Overall budget and its sources; who decides what counts as honest failure                                                                                                                           |
| FSC crowdfunding plan (26 September 2013)  | A financing gap for idea-stage entrepreneurs and costly public-offering rules                                         | Finance, not the viability of ideas, is the constraint; foreign moves to institutionalise crowdfunding are a warrant            | Why angel and early venture investment had fallen; who bears investors’ losses when the ventures fail                                                                                               |
| Second Chances plan (30 October 2013)      | The personal cost of failure – joint guarantees, credit delinquency and stigma – which deters talented people         | Failure can be sorted into honest and opportunistic; easing re-starts raises start-ups                                          | Who bears the residual risk of waived guarantees; the definition of honest failure                                                                                                                  |

Source: IFEED analysis after Rochefort and Cobb (1993) and Bacchi (2009) of SMBA (25 March 2013); FSC (3 April 2013); Government of the Republic of Korea (15 May 2013, 5 June 2013); FSC (26 September 2013); Government of the Republic of Korea (30 October 2013).

## 3.2 THEORETICAL ANALYSIS: THEORETICAL VALIDITY AND RELEVANCE

Table 3 sets the main policies of 2013 against the theories that bear on them: whether the mechanism on which each relied is one that research supports, and whether it addressed the conditions that research finds relevant.

Measured against ecosystem theory, the policy mix as a whole had low relevance. Isenberg treats policy, finance, culture, supports, human capital and markets as interdependent domains and warns against emulating Silicon Valley (Isenberg, 2010, 2011); studies of new clusters find that firm-

building capabilities, skilled labour and connection to markets start a new entrepreneurial region (Bresnahan et al., 2001), and that venture capital and support services lag rather than lead an entrepreneurial culture built by pioneering entrepreneurs (Feldman, 2001). The policy of 2013 began instead with the features of a mature cluster – venture funds, angel investors, exit markets – and the government compared Korea with other countries on the size of angel investment and the rates of tax relief and took its models from abroad – the US crowd-sourcing company Quirky, the Israeli incubator programme and a US start-up visa bill (Government of the Republic of Korea, 15 May 2013, plan, pp. 8–9, 20, 39, 44) – so that borrowing from abroad ran the risk of incomplete and inappropriate transfer, taking instruments without the conditions that made them work in their places of origin (Dolowitz & Marsh, 2000). The measures for education, incubation and public demand were relevant in theory but small.

Finance theory gives a more mixed verdict. Lenders ration credit to firms whose risk they cannot observe (Stiglitz & Weiss, 1981), which gives guarantees a rationale; but a guarantee is justified chiefly by its incrementality, the share of guaranteed loans that would not otherwise have been made (Riding et al., 2007), and no plan estimated it. Public venture capital works best when it complements private investors and leaves investment choices to them (Lerner, 2002, 2009), which the incubator-linked programme did; tax-subsidised, government-sponsored funds, on the other hand, can crowd out other venture capital (Cumming & MacIntosh, 2006), a risk that the funds' public anchoring and priority returns raised and that no plan examined. Lerner also identifies as a frequent fault of public programmes the presumption that technological criteria can be separated from business considerations (Lerner, 2002), and several instruments of 2013 risked that fault where they selected firms by technology grade (FSC, 3 April 2013, reference material, pp. 18–19; Government of the Republic of Korea, 30 October 2013, plan, p. 12).

On failure, a real options perspective supports lowering the cost of failure, since an entrepreneur-friendly treatment of failure can encourage riskier, higher-return ventures (Lee et al., 2007); the abolition of joint guarantees and the shorter credit records were valid in these terms. The test of honest failure was not (Section 2.3.2): a design that rewards groups constructed as deserving and burdens those constructed as suspect tends to reinforce the construction (Schneider & Ingram, 1993). On targeting, Shane (2009) argues that encouraging more people to found firms is bad policy and that support should go to the few with growth potential, and Mason and Brown (2013) that high-growth firms cannot be found by targeting sectors, technologies or types of firm; the plans of 2013 nonetheless measured progress by the number of start-ups and new incorporations (SMBA, 25 March 2013, 15 October 2013).

**Table 3: Theoretical validity of the main policies**

| Policy                                                                  | Theory                                                                                                                                                                    | Assessment        | Reason                                                                                          |
|-------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|-------------------------------------------------------------------------------------------------|
| Abolition of joint guarantees; shorter credit records                   | Lowering the cost of failure can encourage entry and risk-taking (Lee et al., 2007)                                                                                       | Consistent        | Removed personal liabilities that deter entry                                                   |
| Staged waiver of founders' guarantees; "honest failure" test for relief | Failure is attributed to misfortune or mistakes (Cardon et al., 2011); designs tend to reinforce constructions of deserving and suspect groups (Schneider & Ingram, 1993) | Partly consistent | Right aim, but a moral gate preserves stigma                                                    |
| Incubator-linked R&D matched to angel investment                        | Public venture capital works when it complements private investors (Lerner, 2002)                                                                                         | Consistent        | Private operators select; public money follows private money                                    |
| Future Creation, Growth Ladder and youth start-up funds                 | Tax-subsidised, government-sponsored funds can crowd out private venture capital (Cumming & MacIntosh, 2006)                                                              | Partly consistent | Private managers decide, but public anchoring and priority returns; additionality not estimated |
| Guarantees for founders and acquirers                                   | Credit rationing (Stiglitz & Weiss, 1981); incrementality of guarantees (Riding et al., 2007)                                                                             | Partly consistent | A rationale exists, but the lending added was not estimated                                     |
| Angel and M&A tax incentives; KONEX                                     | Interdependent domains (Isenberg, 2010); "old economy" inputs start new clusters (Bresnahan et al., 2001); finance lags culture (Feldman, 2001)                           | Partly consistent | Investor and exit incentives belong to mature clusters                                          |
| Entrepreneurship education; incubation; start-up visa                   | Skills and firm-building capabilities start new clusters (Bresnahan et al., 2001)                                                                                         | Consistent        | Builds human capital and supports, but at small scale                                           |
| Public procurement as "first customer"                                  | Markets are a domain of the ecosystem (Isenberg, 2011)                                                                                                                    | Consistent        | Addresses demand, but apart from the start-up agenda                                            |
| Progress measured by the number of start-ups                            | Quality matters more than number (Shane, 2009); high-growth firms cannot be targeted by type (Mason & Brown, 2013)                                                        | Inconsistent      | Counts founders rather than growth                                                              |
| Silicon Valley, Israeli and foreign crowdfunding models                 | Transfer can be uninformed, incomplete or inappropriate (Dolowitz & Marsh, 2000)                                                                                          | Partly consistent | Instruments borrowed without the conditions that made them work                                 |

Source: IFEED assessment of the policies reviewed in Section 2, against the sources named in the second column.

### 3.3 PRACTICAL ANALYSIS: PERFORMANCE, CONTRIBUTION AND IMPACT

No plan or report of 2013 reported an effect of the policies on firms beyond first firm-level results – KONEX-listed firms raising capital and a few products from the SMBA's idea project (FSC & KRX, 27 December 2013, report, p. 7; SMBA, 15 October 2013, p. 21) – and none could have done more: most measures had been in place for a few months at most. What the government did report was implementation – what had been launched, formed, selected or legislated – and it reported it against the plans' own announcements. Table 4 sets the two side by side for the main finance and market policies.

**Table 4: Announced and reported: funds, programmes, KONEX, tax incentives and guarantees, 2013**

| Policy                             | Announced                                                                                                                                                         | Reported by the end of 2013                                                                                                                                                                                                                                                                                                                              |
|------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Future Creation Fund               | A fund of KRW 500 billion (Government of the Republic of Korea, 15 May 2013, plan, p. 22)                                                                         | KRW 600 billion raised “in only about 2.5 months” after recruitment began; investment to start in mid-September (SMBA, 20 August 2013, p. 1)                                                                                                                                                                                                             |
| Growth Ladder Fund                 | A fund of KRW 2 trillion in the third quarter of 2013, KRW 0.6 trillion of it from policy finance (Government of the Republic of Korea, 15 May 2013, plan, p. 28) | KRW 1.85 trillion committed over three years, KRW 0.6 trillion in the first year, towards a first-year target of KRW 2 trillion with other investors in sub-funds; managers being selected (FSC, 9 August 2013, pp. 1, 3, 11–12)                                                                                                                         |
| Youth start-up funds               | Funds of KRW 100 billion within the year (Government of the Republic of Korea, 15 May 2013, press release, p. 7)                                                  | Kakao and Smilegate funds of KRW 30 billion each, formed in July and September: KRW 60 billion for 2013 (SMBA, 15 October 2013, p. 25)                                                                                                                                                                                                                   |
| Incubator-linked programme         | Full operation from June (Government of the Republic of Korea, 15 May 2013, press release, p. 15)                                                                 | Operators selected in June and 15 teams by December; KRW 6.35 billion of angel investment and government R&D in the first tranche (SMBA, 12 December 2013, p. 2)                                                                                                                                                                                         |
| KONEX                              | Opening in July (Government of the Republic of Korea, 15 May 2013, press release, p. 14)                                                                          | 45 listed firms on 26 December against 21 at opening, short of the 50 targeted, which the review acknowledged and judged good given weak listings on other markets; trading conceded to be thin but assessed as no measure of success (FSC & KRX, 27 December 2013, report, pp. 5, 9–10)                                                                 |
| Angel deduction and M&A tax credit | Within the second half of 2013 (Government of the Republic of Korea, 15 May 2013, plan, pp. 57–58)                                                                | Bills introduced; the M&A credit listed as a new measure, effective 1 January 2014 “provisional, amendment under deliberation in the National Assembly” (MOSF, 26 December 2013, guide, p. 57); the release warned that the guide contained items that could change with the National Assembly’s decisions (MOSF, 26 December 2013, press release, p. 1) |
| Crowdfunding                       | Introduced “within this year” (Government of the Republic of Korea, 15 May 2013, press release, p. 8)                                                             | A plan conditional on passage of the bill within the year, preferably in the regular session; available “from next year at the earliest” (FSC, 26 September 2013, pp. 2, 12)                                                                                                                                                                             |
| Joint guarantees                   | Abolition of third-party joint guarantees in non-bank lending from July (Government of the Republic of Korea, 15 May 2013, press release, p. 18)                  | In force for new contracts from 1 July, with the actual manager of a corporate borrower excepted; staged waiver of founders’ own guarantees announced in three stages from 2013 (FSC & FSS, 26 April 2013, plan, p. 5; Government of the Republic of Korea, 30 October 2013, plan, pp. 11–12; SMBA, 15 October 2013, p. 30)                              |

Source: Government of the Republic of Korea (15 May 2013); SMBA (20 August 2013); FSC (9 August 2013); SMBA (15 October 2013, 12 December 2013); FSC and KRX (27 December 2013); MOSF (26 December 2013); FSC (26 September 2013); FSC and FSS (26 April 2013); Government of the Republic of Korea (30 October 2013).

Three patterns stand out in performance. Where money was to be gathered, the government reported selectively: the Future Creation Fund was larger than planned and its release emphasised the speed with which it was raised (SMBA, 20 August 2013), while the youth start-up funds stood at KRW 60 billion in October against the KRW 100 billion announced for the year, a gap that the SMBA’s report did not mention (Government of the Republic of Korea, 15 May 2013, press release, p. 7; SMBA, 15 October 2013, p. 25); the KONEX review, by contrast, acknowledged that listings had

fallen short of its target (FSC & KRX, 27 December 2013, report, p. 5). Where the policy depended on legislation, it lagged: the larger angel deduction and the tax credit for technology M&A were still before the National Assembly at the end of 2013, although the relief from gift tax for sellers, which needed only a decree, had been made in September; and the crowdfunding bill was pending when the FSC set out its plan (FSC, 26 September 2013, p. 12; MOSF, 26 December 2013, guide, p. 57; SMBA, 15 October 2013, pp. 26–27). And where the policy depended on selecting firms, the government reported selections and amounts – 15 teams chosen by December against 40 projects planned for 2013, two youth funds formed – but not how many firms the new funds had invested in or what had become of the firms (Government of the Republic of Korea, 15 May 2013, plan, p. 39; SMBA, 15 October 2013, p. 25; SMBA, 12 December 2013, p. 2).

The contribution of the other domains was reported in counts: 691 entrepreneurship lectures attended by 92,547 people, Bizcool in 135 schools, 870 teams in customised commercialisation support, four sites of the Youth Start-up Academy, 5,357 ideas leading to six products in production, and 46 business centres for one-person creative enterprises (SMBA, 15 October 2013, pp. 21–23). Counts of this kind show the reach of a programme, not its contribution to the ecosystem; Behn (2003) distinguishes the purposes that performance measures serve – to evaluate, control, budget, motivate, promote, celebrate, learn and improve – and argues that each needs its own measures. The measures reported in 2013 served chiefly to promote and to celebrate.

On impact, the government claimed more than it could show. The SMBA's report to the National Assembly observed that "a climate of investment activity is spreading", citing a 25 % rise in venture investment over the same months of the previous year, and asked in the same sentence for "the related legal amendments" to be "completed quickly" (SMBA, 15 October 2013, pp. 24–25); the rise was measured from January to August, mostly before the May measures could take effect. The FSC's review of KONEX stated that "it is inappropriate to judge the market's success or failure by trading volume" (FSC & KRX, 27 December 2013, report, p. 10) in the passage that conceded thin trading. The argument was consistent with a market designed to restrict trading by individuals (FSC & KRX, 29 June 2013, explanatory material, p. 6), but setting a measure aside at the moment it shows a shortfall is the kind of framing that the politics of blame avoidance would lead one to expect (Weaver, 1986). Yet the policies' own rules would have made evaluation possible: the incubator-linked programme selects teams recommended by operators, the youth start-up funds are limited to young founders and young firms, the Duru Nuri subsidy applies below a pay ceiling in workplaces under a size limit, and the waiver of founders' guarantees was to be introduced in stages (Government of the Republic of Korea, 15 May 2013, 30 October 2013; MOEL & MOHW, 25 March 2013; SMBA, 25 April 2013, 12 December 2013). Each rule divides firms that receive a policy from comparable firms that do not; that no plan or report proposed such a comparison is a gap in accountability, not in data.

Table 5 draws the review and the analysis together by domain. Only the support domain was delivered largely as announced; the others combined measures that worked as intended with measures that awaited legislation, rested on public risk or were not linked to new firms.

**Table 5: Assessment of the policies by domain**

| Domain             | Main policies                                                                                                                                                                                  | Performance by the end of 2013                                                                                                                                   | Assessment |
|--------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------|
| Regulation and law | Joint guarantees abolished in non-bank lending; venture capital sanctions; tax relief and shorter credit records for re-starters; founders' guarantee waiver and fast rehabilitation announced | Most rules in force within the year and sound; the founders' waiver beyond its first stage and the fast procedure still planned, and relief tied to a moral test | Mixed      |
| Finance            | KRW 600 billion Future Creation Fund; KRW 1.85 trillion committed to the Growth Ladder Fund; KRW 60 billion of youth funds; 15 incubator-linked teams; new guarantees and re-start loans       | Money mobilised quickly on public risk; investor incentives and crowdfunding awaited legislation                                                                 | Mixed      |
| Culture            | Lectures, forums and auditions; re-start campaigns and conferences; relief reserved for "honest failure"                                                                                       | Wide reach in events; stigma given an administrative basis                                                                                                       | Mixed      |
| Support            | Youth Start-up Academy and prototype workshops expanded to four sites each; Creative Economy Town; global start-up programmes                                                                  | Largely delivered as announced, at small scale; the idea funnel thin                                                                                             | Good       |
| Human capital      | Entrepreneurship education from schools to universities; five-year plan for universities; start-up visa; minimum wage and Duru Nuri subsidy                                                    | Education plan adopted; labour costs left outside start-up policy                                                                                                | Mixed      |
| Market             | Public procurement measures; KONEX; M&A rules eased and tax credit pending                                                                                                                     | KONEX opened; demand measures apart from the start-up agenda; main exit incentive pending                                                                        | Mixed      |

Source: IFEED assessment of the policies reviewed in Section 2, on the sources cited there.

## 4 POLICY LIMITATIONS

### 4.1 POLICY DEBATES, CONTESTED POINTS AND ISSUES

The policies of 2013 raised questions that the plans and reports did not settle and that later policy would have to answer. Table 6 sets out the main ones, each with what the government said and the point at issue.

**Table 6: Debates and contested points in the policies of 2013**

| Issue                              | What the plans and reports said                                                                                                                                                                                                                                                                                                                                                                                                                                                  | Point at issue                                                                                           |
|------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------|
| Investment or loans?               | Promised start-ups financed by “investment, not loans”, while adding a 100 % guarantee for prospective founders and guarantees for acquirers’ loans (Government of the Republic of Korea, 15 May 2013, 5 June 2013)                                                                                                                                                                                                                                                              | Whether the guarantees added lending that would not otherwise have been made, or kept start-ups on loans |
| Private leadership or public risk? | Priority returns for private investors, a capped public first-loss account planned in May and policy finance bearing “more of the investment risk” (FSC, 3 April 2013; Government of the Republic of Korea, 15 May 2013; SMBA, 20 August 2013)                                                                                                                                                                                                                                   | How large the losses of public money could be, and whether private money was added or merely subsidised  |
| Who counts as an honest failure?   | Preferential re-start track and debt relief limited to “honest failure”; the criteria left to a study (Government of the Republic of Korea, 30 October 2013)                                                                                                                                                                                                                                                                                                                     | Who decides, on what evidence, and whether the test reproduces the stigma it was meant to remove         |
| Who gains from the tax incentives? | A 50 % angel deduction illustrated by an investor who puts KRW 50 million a year into a venture (Government of the Republic of Korea, 15 May 2013; SMBA, 15 October 2013)                                                                                                                                                                                                                                                                                                        | Whether the incentive reaches beyond high-income investors                                               |
| Announced before enacted           | Angel and M&A incentives and crowdfunding announced for 2013 but still bills at the end of 2013; the M&A credit listed as a new measure for 2014, marked “provisional” (FSC, 26 September 2013; MOSF, 26 December 2013; SMBA, 15 October 2013)                                                                                                                                                                                                                                   | The credibility of announcements, and the listing of pending measures among the year’s changes           |
| Large companies and start-ups      | Large acquirers to be given three years, under a decree notified in October, before an acquired venture counts as an affiliate, with immediate inclusion where the acquired firm invested in group affiliates, gave debt guarantees or engaged in unfair internal transactions, while the May plan treated the taking of technology by large firms as a threat to small firms (Government of the Republic of Korea, 15 May 2013, plan, pp. 12, 26; SMBA, 15 October 2013, p. 27) | Whether easier acquisition helps start-ups exit or concentrates technology in large groups               |
| How many start-ups?                | Progress measured by the number of start-ups and new incorporations (SMBA, 25 March 2013, 15 October 2013)                                                                                                                                                                                                                                                                                                                                                                       | Whether the aim is more founders or more firms that grow                                                 |

Source: IFEED analysis of Government of the Republic of Korea (15 May 2013, 5 June 2013); FSC (3 April 2013); SMBA (20 August 2013); Government of the Republic of Korea (30 October 2013); SMBA (15 October 2013); FSC (26 September 2013); MOSF (26 December 2013); SMBA (25 March 2013).

Two of these debates go to the heart of the year's policy. The first is the balance between private leadership and public risk: the narrative of a circle turned by successful investors rested on designs in which the public balance sheet carried much of the risk and private investors much of the upside, and no plan set out the expected losses of public money. The second is the distribution of relief from failure: the government sought to lift the stigma of failure while making relief depend on a judgement of honesty, a tension that it left to a study and that the policies of 2014 would have to resolve.

## 4.2 THEORETICAL LIMITATIONS OF THE POLICIES

Beyond the debates over single measures, the policy mix of 2013 rested on a theory of change with three limitations. First, it assumed that an entrepreneurial ecosystem could be built by money: it defined the problem by the structure of finance (Rochefort & Cobb, 1993) and largely reduced Isenberg's interdependent domains to the stages of a circuit of money – start-up, growth, exit, reinvestment (Isenberg, 2011). In the May plan, the measures for ideas, talent and information were related to that circuit only as its “infrastructure” for “the smooth flow of venture funds” (Government of the Republic of Korea, 15 May 2013, plan, p. 38), and the policies for culture, supports, human capital and markets reviewed in Section 2 were small beside the funds and tax incentives.

Second, it assumed that the instruments of mature clusters would start a new one, reversing the order that the cluster literature describes (Section 3.2). For the policy as a whole this created a problem of time: the stages that were to close the circle – exits, and reinvestment by “successful seniors” – lay years beyond the funds formed in 2013, so that whether the borrowed instruments fitted Korean conditions (Dolowitz & Marsh, 2000) could not be known within the period in which they were announced.

Third, it had no theory of growth or of demand. It counted start-ups rather than asking which firms would grow (Mason & Brown, 2013; Shane, 2009), and it treated customers as something the state could supply as a “first customer” rather than as the market in which new firms must succeed. A policy built on these assumptions could report outputs, but it could not say how they would add up to an ecosystem.

## 5 POLICY IMPLICATIONS

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The review and the analysis point to directions for improving the policy. For finance, the start-up problem should be defined more broadly than as a shortage of money, to include the markets in which new firms must sell and what limits their growth once founded (Rochefort & Cobb, 1993). The allocation of risk should be stated when funds are launched – who bears the losses of public money and guarantees, and who receives the returns – and each guarantee and public co-investment should be justified by the finance it adds rather than displaces (Cumming & MacIntosh, 2006; Riding et al., 2007). The balance between loans, guarantees and investment should be made explicit and reported each year, so that the promise of “investment, not loans” can be checked.

For failure, relief should rest on published criteria for honest failure, applied transparently and with the number of applicants refused reported, if it is not to reproduce the stigma it is meant to remove (Cardon et al., 2011; Schneider & Ingram, 1993); the measures that lower the cost of failure for everyone, such as the abolition of joint guarantees and shorter credit records, deserve priority over measures that ration relief by a moral test. For legislation, announcements should be sequenced with the bills they need, and measures still pending should be reported as pending.

For the other domains, policy should treat education, supports, culture and markets as domains of their own rather than as infrastructure for finance (Isenberg, 2011). Public procurement should be opened to new firms, not only to SMEs in general; the education and incubation programmes, which were among the better policies of the year, should be judged by what becomes of the founders and firms they serve; and start-up policy should take account of the labour costs that the minimum wage and the Duru Nuri subsidy set for every new employer.

For accountability, since different purposes require different measures (Behn, 2003), measures should be chosen that serve to evaluate and to learn, not only to promote, and the policies’ own selection rules – operators’ recommendations, preliminary technology assessments, age limits and staged waivers – should be used to compare supported firms with similar firms that were not supported. Above all, as Isenberg (2010) argued, no single domain, and no foreign model, can stand in for the ecosystem: ideas, people and markets need policies of their own beside the circuit of money.

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