

## A Structural Hole in Social Enterprise Networks: Are You Our Friend or Stranger?

Sanghee Han  
Sogang Business School, Sogang University

Young Kyun Chang  
Sogang Business School, Sogang University  
youngkyunchang@gmail.com

### Abstract

*This study proposes that social enterprise networks are closed networks based on clan economy and strong identities shaped by the unique challenges of low economic viability and external scrutiny for their dual missions. As such, within the networks, structural hole spanners who actively interact with various actors can be treated as a stranger by within-network members, and thus benefit less from the networks. With 363 observations of social enterprises in Korea collected between 2021 and 2022, we found that the structural hole position in social enterprise networks made it more difficult to obtain capitals from external sources. In addition, we also found that, beyond a certain threshold, the greater the external resources obtained, the poorer the financial performance of the social enterprises. This study is meaningful in challenging the common assumptions of the social network literature in the context of social enterprises.*

**Keywords:** *Social Enterprises, Social Networks, Structural holes, External Resources*

### 1. Introduction

Social enterprises have been gaining attention as an alternative to market failures, as they address social problems in an entrepreneurial manner (Austin, Stevenson, & Wei-Skillern, 2006). Nevertheless, social enterprises are confronted with the challenge of pursuing both social and economic goals simultaneously. They often encounter difficulties in procuring greater financial resources and in managing these resources effectively. At the same time, they must prove themselves to be legitimate by demonstrating their commitment to social values. Due to the difficulty

and complexity of achieving double objectives, social enterprises tend to rely on their networks.

However, to date little is known about how social enterprises behave in the network structure. This paper focuses on “structural holes” in a social enterprises network structure. This study particularly examines whether structural holes are advantageous or disadvantageous of procuring funds from external sources. Furthermore, this paper also examines if external funding really contributes to the firm’s financial performance.

This study contributes to the literature in the following ways. First, this study expands the theorization boundary of network theory to the area of social entrepreneurship. Given the clan-like nature of social enterprise networks, our approach offers novel understanding of how social enterprises behave in the network structure. Second, this study challenges the common wisdom that successful entrepreneurial firms tend to utilize more external resources than unsuccessful ones (Jarillo, 1989). We empirically examine if external funding really contributes to enhance social enterprises’ financial performances. Last, this study contributes to knowledge management literature by providing relevant rationales and evidence of how critical information (i.e., information about external funding) could be transferred within a highly cohesive network.

### 2. Hypotheses

#### 2.1. The structural holes in social enterprise networks

Granovetter (1985) posited that individual economic behavior is embedded in social structures. He contended that both economics’ attempts (explaining economic behavior as the self-interested actions of atomized

individuals) and sociology's attempts (explaining economic behavior as entirely driven by social customs and norms) only partially explain the phenomenon. According to Granovetter, individuals are not solely driven by self-interested motives to realize economic benefits through 'rational' transactions in the marketplace. Rather, factors in social relationships (e.g., trust) that are often viewed as irrational influence transactions in the marketplace. Uzzi (1999) subsequently refined the definition of embeddedness, which is "the degree to which commercial transactions take place through social relationships and networks of relationships that use exchange protocols associated with social, noncommercial ties to govern business transactions (p. 482)."

The concept of embeddedness has since become a central theme in the development of social capital and network theory. According to social capital theory, in contrast to physical capital, social capital is a resource that is made available to actors by the structure of their relationships with each other, i.e., networks (Adler & Kwon, 2002; Bubini & Aldrich, 1991). The efforts of actors to form relationships are rewarded through social capital, which can be categorized into three forms: information exchanged in the network, power (influence) in the network, or superior access to ties (Adler & Kwon, 2002).

Granovetter's (1973) breakthrough work on the "strength of weak ties" implies the importance of social networks. Unlike the strong ties that bind clique of actors together and primarily convey private information, weak ties are sources of new information since they connect local networks. Thus, an individual who has more weak ties in the network is likely to have less redundant and more diverse information. Similar to the concept of weak ties, Burt (1992) later used the term "structural hole" to indicate the absence of connections among actors in the network. Burt argued that the more structural holes surrounding an actor, the more useful the network is. In short, early theorists, like Granovetter and Burt, concluded that sparse networks could be more advantageous to individuals in mobility contests. And since then, social network researchers have repeatedly concluded that structural holes are beneficial to actors (Goduscheit, Khanin, Mahto, & McDowell, 2021; Wen, Qualls, & Zeng, 2021).

However, later Podolny and Baron (1997) challenged the benefit of weak ties or structural holes. As Granovetter and Burt proposed, material resource flows are better utilized when they are conveyed through sparse networks. However, if the resources are *identity-based* contents (e.g., normative expectations, social identities), there are clear advantage to a more "cohesive" network (Podolny & Baron, 1997). This is because a cohesive network conveys a clear normative

order within which individuals can optimize their behavior without having conflict preferences. This claim hints at the idea that structural holes could be disadvantageous to individuals when the networks are cohesive and key contents being flowed are identity-based ones.

In this study, we define social enterprise network as a cohesive, closed network. We insist that social entrepreneurs tend to tightly bind together, and seek to maintain their organizations by virtue of sharing a strong sense of social identity.

Here are the reasons. First, Social enterprises tend to pursue both social and economic values, while seeking viability. Their dually purposeful behaviors are often subject to the scrutiny of their stakeholders. In reality, social enterprises often compromise social gains in order to create economic value. However, it is extremely difficult for an individual firm to survive in a highly competitive market economy where corporations can survive by achieving both better economic performance and social value. Therefore, due to their inherent weak competitiveness, social enterprises are likely to rely on their own *clan-like* economy (vs. market economy) by focusing more on interdependence and reciprocity among members (Minbaeva & Muratbekova-Touron, 2013) rather than independent and competition.

In this unique context, social enterprises in a structural hole position who interact actively with outsiders would be less interdependent and more independent from within-network actors. As a result, they would benefit less from their networks, as they might be isolated from the valuable information and resources circulating within this closed economy.

Second, social enterprise networks can be sustained by a strong sense of social identity. The most useful contents in any networks are materials, resources, and information that can contribute to an individual's economic wealth. However, as Podolny and Baron (1997) mentioned, individuals in a "cohesive network" (like a social enterprise network) could benefit more from *identity-based contents*, such as social missions, conscious business, public service motivation, and so on. Within this unique value-laden network, a clear normative order is conveyed, so that individuals can optimize their behavior without having conflict preferences.

However, social enterprises who are positioned in a structural hole and interact with others in more open, broader networks may *act differently*. They often deviate from norms and identities that their networks exactly dictate. This behavior can be perceived by network members to be "mission drift" (Jones, 2007; Cornforth, 2014; Ebrahim, Battilana, & Mair, 2014). As such, they would be disadvantageous of having valuable information and resources within the networks

Taken together, social enterprises positioned in a structural hole would be treated as a “stranger” (rather than a “friend”) from within-network members. Thus, social enterprises in the structural hole position is disadvantageous of having valuable information and resources flowed within the networks, including the information about external funding sources and opportunities (e.g., who has available funds, how to access them). As such, we develop our first hypothesis:

*H1: Social enterprises positioned in structural holes within the social enterprise network will secure fewer capitals from external sources.*

## **2.2. The effect of procurement for external resources on firm performance**

Funding is a universal phenomenon observed in all entrepreneurial firms. External resources are defined as “those assets-physical or otherwise-that are used by the firm in its pursuit of growth and over which the firm has no direct ownership (Jarillo, 1989: 135).” It has been well recognized that fast-growing entrepreneurial firms tend to utilize more external resources than slower-growing ones (Jarillo, 1989).

Social enterprises are not exception. Social enterprises are heavily dependent on external resources for their survival (Aldrich & Zimmer, 1986; Jarillo, 1989). But the unanswered question is: *Does social enterprises’ dependence on external resources (e.g., funding) really help to perform better as other entrepreneurial firms do?*

In this study, we hypothesize that social enterprises will exhibit the highest performance when they procure the “moderate” level of external resources, and that they will exhibit lower economic performance when they procure either too few or excessive external resources. When social enterprises procure the moderate level of external resources, they are able to leverage resources to seize opportunities and achieve a competitive advantage.

However, social enterprises with a higher level (vs. moderate level) of externally procured resources will exhibit lower firm performance. Several prior studies on social enterprises have already noted that social enterprises may not utilize resources efficiently due to the intervention of external resource providers (Adams & Perlmutter, 1991; Austin et al., 2006). Specifically, according to Austin et al. (2006), social enterprises must continue to receive funding from outside sources due to the low economic viability of the business. In return, external funders ask a number of demands on social enterprises, which “can impose significant limitations on a social entrepreneurs’ ability to determine how

resources can best be deployed to reach organizational goals (p.15).”

For example, when receiving funding from the government, social enterprises face additional costs for administrative processing and are compelled to operate their enterprises in a less efficient manner by deploying resources in order to meet the conditions of the funding (Adams & Perlmutter, 1991). Therefore, based on the above discussion, we develop our second hypothesis:

*H2: There will be an inverted U-shaped relationship between the level of procured external funding and their financial performance.*

## **3. Methodology**

### **3.1. Sample and data**

The sample of this study consists of social enterprises who participated in the supporting program sponsored by SK, one of largest business groups in South Korea, between 2020 and 2022. Since 2015, SK has been implementing the Social Progress Credit (SPC) program, which measures the social performance of participating social enterprises by monetary value and provides monetary incentives according to the level of performance (Jung & Shin, 2022). SK has collected various data from social enterprises participating in the SPC program. The data used here to test our hypotheses include the balance sheets and income statements, as well as social enterprises’ CEOs responses to the annual survey. The sample size is 224 in 2021 and 254 in 2022. After excluding missing data, the number of observations for analysis was 363.

It should be noted that the sample in this study covers a wide range of industries, business models, and stages of development. In particular, our sample is distributed across 16 industries according to the 10th Korean Standard Industrial Classification (21 industries in total), and are at different stages of the social enterprise lifecycle, ranging from those established in 1982 to those established in 2021. Moreover, the program categorizes various different social enterprises models based on both their stated missions and the means by which they achieve social performance. Each category is further divided into four subcategories: social service outcomes, employment outcomes, social ecosystem outcomes, and environmental outcomes.

In short, although the sample of this study is limited to participating firms in a specific sponsoring program, it seems to represent the characteristics of a larger population of social enterprises in Korea.

### 3.2. Compositing quasi-network data

In this study, we employed a method of constructing quasi-network data to identify social enterprise networks. In the field of social network research, network data is typically constructed through the surveys that include a question designed to list up the names of other actors (e.g., *please name up to five people you know in order of importance*). However, this approach is only viable when surveys are designed with the specific objective of network analysis in advance and is not applicable to secondary archival data. The quasi-network approach employed in this study addresses this limitation by utilizing data on actors' characteristics (e.g., demographics) or behaviors (e.g., participation in a particular event) to identify interactions among actors.

The quasi-network approach postulates that if two actors possess similar characteristics or have a history of participating in the same events, they would likely to have meaningful interactions. Accordingly, when constructing a quasi-network, it is recommended that data on events (e.g., social gatherings, co-sponsoring a bill, etc.) in which the two actors participated together be included. This is because it is relatively clear that the two actors would have interacted in these events, thereby providing a basis for assuming the validity of the quasi-network approach. It is also widely acknowledged that actors with similar demographic characteristics are likely to interact within a network (Balliet, Wu, & De Dreu, 2014). Accordingly, in this study, the demographic characteristics of social enterprise CEOs are also included for the network analysis.

In order to construct the quasi-network data, a total of six characteristics were taken into consideration: (1) length of participation in the SPC program, (2) experience with angel or accelerator funding, (3) whether the CEO is a founder, (4) CEO age, (5) CEO gender, and (6) CEO education level. The first two characteristics represent events that social enterprise CEOs have collectively participated in. The others were included on the basis of prior research indicating that people are more likely to interact positively (i.e., favoritism) when they feel a greater sense of identification based on the similar characteristics (Tajfel, 1979).

The quasi-network data were organized as follows: First, the dissimilarity between two CEOs was calculated using the Euclidean distance metric based on the six characteristics of each CEO. This process was repeated for all CEO dyadic, resulting in a 363 x 363 matrix of Euclidean distance values. Then, the Euclidean distances of all CEO pairs were averaged. Based on this average value, it was assumed that only

closer CEOs (Euclidean distance values below the average) were networking with each other (see Borgatti & Everett, 1997; Kim & Kim, 2016). The 363 x 363 matrix was converted into an adjacency matrix by coding CEO dyadic with values below the average as 1 and CEO dyadic with values above the average as 0. This transformed matrix is the quasi-network data.

### 3.3. Measurement

**3.3.1. Structural hole.** It was measured by the *Constraint* proposed by Burt (1995). The equation for calculating Constraint is as follows:

$$C_i = \Sigma_j \left( p_{ij} + \sum_{q=1}^h p_{iq} \cdot p_{qj} \right), \quad p \neq i, j$$

Where  $p_{iq}$  equals the strength of direct ties from  $i$  to  $j$ , and  $\sum p_{iq}p_{jq}$  is the sum of the indirect tie strength from  $i$  to  $j$  via all  $q$  (Zaheer & Bell, 2005). However, in this study, 2 minus Constraint is used in the analysis for ease of interpretation (Choi & Zo, 2022).

**3.3.2. Level of procurement of external resources.** It was measured based on the survey conducted in year  $t$ . Each CEO described a funding information with a percentage of each source, assuming a total sum is 100. The funding sources include (1) *Operating income*, (2) *Non-operating income*, (3) *CEO's personal money*, (4) *Friends and relatives*, (5) *Angel investment*, (6) *Venture capital*, (7) *Corporate bonds*, (8) *Government policy funds (including government grants and loans)*, (9) *Bank corporate loan*, (10) *Bank personal loan*, (11) *High-interest loans*, (12) *Other source*. Since (1) to (3) are not related to external funding, only (4) to (11) sources were summed up to measure the level of procurement of external resources. If it was a kind of an external resource, (12) was also added.

**3.3.3. Financial performance.** It was measured by return on assets (ROA), i.e., profit before taxes divided by total assets.

**3.3.4. Control variables.** Controls were included, such as various CEO characteristics, firm's previous year performance and firm characteristics. Specifically, the CEO characteristics variables are CEO founder status (*Founder CEO*), *CEO age*, *CEO education level*, and *CEO gender*. The firm's previous year performance was measured with R&D expenditure of year  $t-1$  (*Priori R&D*) and ROA of year  $t-1$  (*Prior performance*). The firm characteristics variables are *Firm size*, *Firm age*, *Industry*, *Firm type*, *Social enterprise certification*, and prior experiences of angel investment or accelerator funding (*Funding experiences*).

Figure 1. Social enterprise networks in 2021

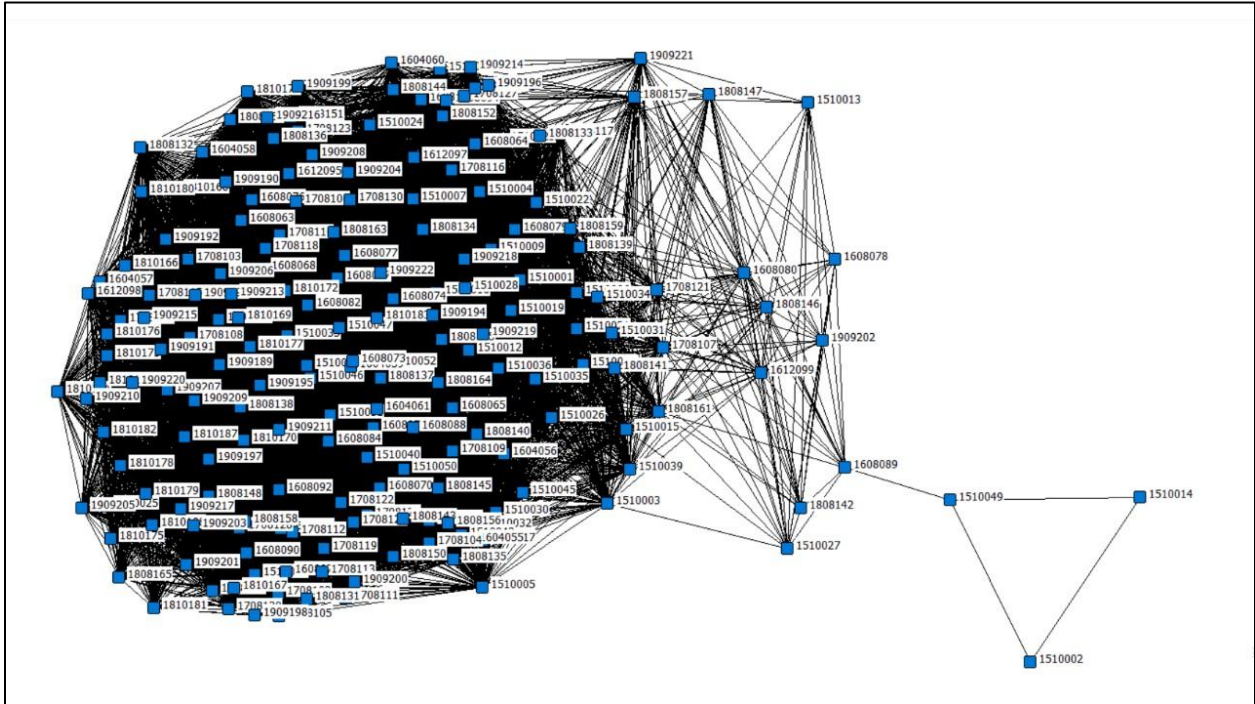
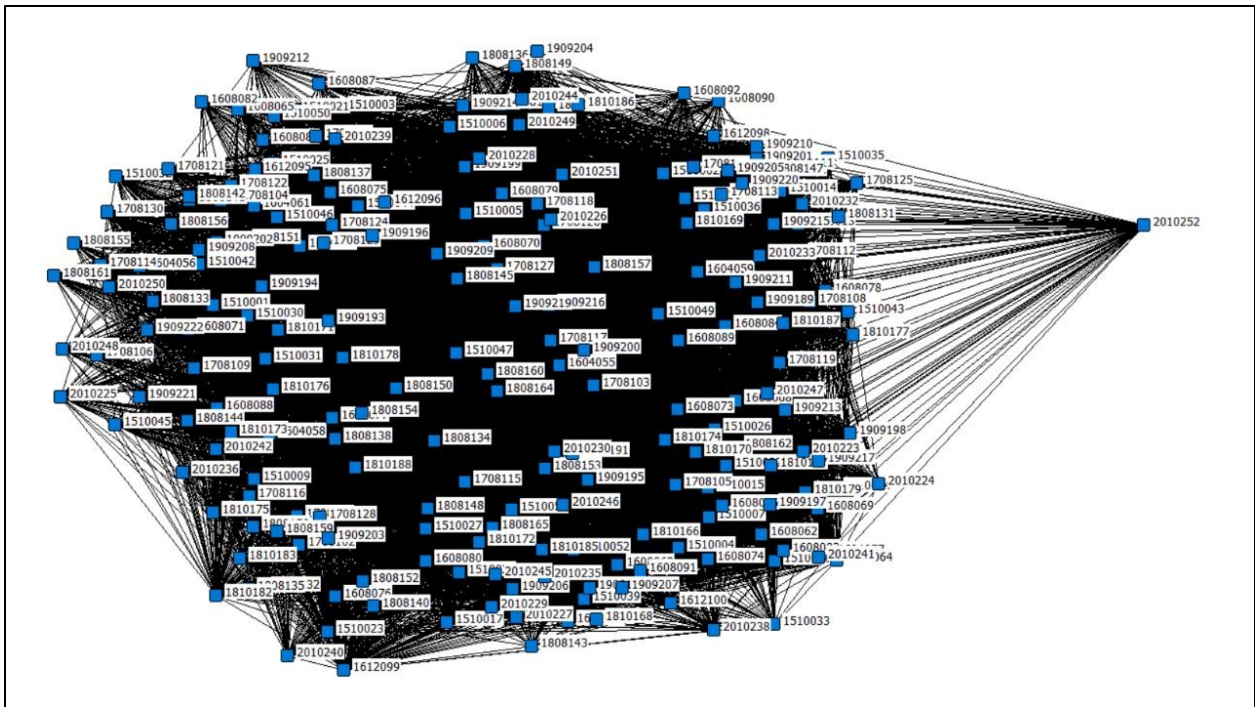


Figure 2. Social enterprise networks in 2022



**Table 1. Descriptive statistics**

Variable	Mean	S.D.	1 Q	Median	3 Q
Firm size	4.52	0.29	4.32	4.51	4.75
Firm age	2.23	0.40	1.95	2.30	2.48
Prior performance	-0.02	0.22	-0.12	0.01	0.10
Prior R&D	0.03	0.07	0.00	0.00	0.01
Structural hole	1.97	0.01	1.97	1.97	1.97
The procurement of external resources	0.35	0.33	0.0	0.3	0.6
Firm performance	-0.03	0.22	-0.12	0.01	0.08

**Table 2. Correlations**

	(1)	(2)	(3)	(4)	(5)	(6)
(1) Firm size	-					
(2) Firm age	0.09	-				
(3) Prior performance	0.14*	0.07*	-			
(4) Prior R&D	-0.06	-0.13**	-0.02	-		
(5) Structural hole	0.03	0.03	0.01	0.03	-	
(6) The procurement of external resources	0.30**	0.14**	-0.26**	0.11**	-0.07	-
(7) Firm performance	0.10*	0.12**	0.39**	-0.14**	0.02	-0.24**

Note: n=363, † p<.10, \* p<.05, \*\* p<.01

**Table 3. The result of hierarchical regression**

	DV: The procurement of external resources				DV: Firm performance					
	Model 1		Model 2		Model 3		Model 4		Model 5	
	$\beta$	t	$\beta$	t	$\beta$	t	$\beta$	t	$\beta$	t
Intercept	-0.69	-1.89†	8.69	0.10	-0.29	-1.12	-0.36	-1.39	-0.49	-1.93†
Firm size	0.20	3.36**	0.19	0.00**	0.07	1.61	0.09	2.07*	0.09	2.23*
Funding experiences	-0.17	-3.51**	-0.17	0.00**	0.13	3.70**	0.11	3.18**	0.12	3.41**
Prior performance	-0.27	-3.62**	-0.29	0.00**	0.24	4.32**	0.21	3.78**	0.19	3.56**
Founder CEO	-0.08	-2.17*	-0.08	0.03*	-0.02	-0.71	-0.03	-1.02	-0.02	-0.95
CEO gender	-0.10	-2.95**	-0.09	0.01**	0.00	-0.07	-0.01	-0.48	-0.01	-0.46
Structural hole			-4.73	0.08†						
The procurement of external resources							-0.10	-2.63**	0.35	3.30**
The procurement of external resources <sup>2</sup>									-0.51	-4.55**
Adjusted R <sup>2</sup>	0.32		0.32		0.23		0.25		0.29	
F-value	6.68**		6.16**		4.60**		4.74**		5.47**	

Note: n=363, † p<.10, \* p<.05, \*\* p<.01; Industry, Firm type, Firm age, Firm certification, Prior R&D, CEO age, and CEO education level were included in the analysis as control variables but are not reported in this summary for the sake of brevity.

For *Social enterprise certification*, Korea has enacted the Social Enterprise Promotion Act (2012), which supports social enterprises with financial aid, tax reduction, and other benefits when firms are certified.

### 3.4. Analysis and results

To prevent erroneous results due to outliers, all continuous variables employed in this analysis have been winsorized at the 5% and 95% percentiles. UNICET 6.791 was employed to construct the social enterprise network, visualize it (see Figures 1 and 2) and calculate the degree to which each CEO is situated within the structural hole (Borgatti, Everett, & Freeman, 2002). R 4.3.0 was utilized for basic statistical analysis, correlation analysis, and regression analysis. The basic statistics and correlation coefficients of the study sample are presented in Tables 1 and 2. The Variance Inflation Factor (VIF) calculated based on firm size was 1.006, which is less than 5, indicating that multicollinearity among the independent variables is not a problem.

The results of the hierarchical regression analysis are shown in Table 3. Model 2 shows that firms located in *Structural hole* in the social enterprise networks have a lower *procurement of external resources* than those who are not in that position ( $\beta = -4.73, p < .10$ ). Therefore, Hypothesis 1 is supported.

For H2, Model 5 tests the relationship between the *procurement of external resources* and *Firm performance*, showing a positive and significant first-order term ( $\beta = .35, p < .01$ ) and a negative and significant second-order (squared) term ( $\beta = -.51, p < .01$ ) on *Firm performance*. The *procurement of external resources* and *Firm performance* of social enterprises exhibited an inverted U-shaped relationship. Thus, Hypothesis 2 was also supported.

## 4. Discussion

### 4.1. A summary of findings

This study reports two interesting findings. First, unlike the most previous studies that have reported a positive role of structural holes, our analysis indicates that structural hole position in social enterprise networks have a negative effect on social enterprises' external resource procurement.

This finding seems to be associated with the unique characteristics of social enterprise networks. Social enterprise networks are known for being cohesive and closed, where social entrepreneurs form tight bonds and maintain their organizations through a shared sense of "social" identity. These networks aim to

balance social and economic values, but often compromising social values in order to seek economic gains. This dual objective makes it challenging for individual firms to survive in a competitive market. This leads to social enterprises relying on a clan-like economy that prioritizes mutual assistance and reciprocity among members over independent competition. Social enterprises located in structural hole positions are likely to interact more with outsiders. But they tend to be less interdependent with network members, resulting in fewer benefits and potential isolation from valuable information and resources.

Moreover, these networks are sustained by a strong sense of social identity, with normative content often including social missions and public service motivations rather than purely economic resources. This cohesive structure helps individuals align their behavior with shared norms and values. However, social enterprises that engage with broader, outward networks may deviate from these norms, facing disadvantages in accessing valuable network resources. Ultimately, social enterprises in structural hole positions are often seen as "strangers" within their networks, limiting their access to crucial information such as external funding sources.

Second, our analysis indicates that social enterprises tend to perform less when they procure too little or too much external funds, whereas to best perform when the level of funding is moderate. This finding is also contrary to the common wisdom, which posits that successful entrepreneurial firms tend to utilize more external resources than unsuccessful ones (Jarillo, 1989).

In fact, extant research has already indicated that social enterprises often do not utilize resources efficiently due to the intervention of external resource providers (Adams & Perlmutter, 1991; Austin et al., 2006). For instance, when social enterprises receive government funding, they incur additional administrative costs and must often allocate resources inefficiently to comply with funding conditions (Adams & Perlmutter, 1991).

### 4.2. Implications

The findings of this study have several implications. First, this study contributes to the social capital and social network literature by providing empirical evidence that the effect of structural holes may depend on the characteristics of the network. This reminds us of the need to carefully examine boundary conditions in related studies. Burt (1995) proposed that the degree of advantage derived from structural holes might be contingent upon individual

motivations; however, he also asserted that the level of analysis or the nature of the unit of analysis is already inherent within the network structure itself. Nevertheless, the findings of this study indicate that the utility of structural holes may be depends on the nature of the relationship and the structure of networks (Gargiulo & Benassi, 2000; Podolny & Baron, 1997).

Second, this study contributes to the social network literature by using quasi-network approach, thereby extending the applicability of social network analysis methodology. The quasi-network data was constructed by calculating the dissimilarity between CEOs based on their characteristics. The assumption behind this method is that individuals in the network might be willing to interact based on similarities (vs. differences). Although numerous studies have used the direct survey method to capture the networks, this study attempts to transform the secondary archival data (CEO's demographic data) into a network analysis-ready dataset.

Last, this study contributes to the existing literature on social entrepreneurship by providing empirical evidence that an excessive inflow of external resources may harm social enterprise performance. This result calls into question the common wisdom of the entrepreneurship literature, and highlights the necessity for a more critical examination. The findings of this study indicate that social enterprises may only be able to achieve a competitive advantage when they receive an optimal level of external resources. If resources are deficient or excessive, social enterprises would perform poorly. Consequently, this study proposes an important practical implication that social enterprises should seek self-sufficiency first, not simply relying on external resources. Also, external institutions and government should be more conscious of offering funds to social enterprises, with a careful look whether they are excessively funded or not.

#### 4.3. Limitations and future research

This study did not directly measure the network ties between enterprises. Instead, this study used quasi-network data by calculating the dissimilarity (Euclidean distance) between CEOs based on their key characteristics. Our approach is practical and general-purpose, but may not fully capture the nuances of the interactions between CEOs. This is a major limitation. Future studies need to confirm the results of this study by directly measuring the relationship tie between CEOs of social enterprises.

Furthermore, this study used a sample of social enterprises that participated in a specific sponsoring program. As such, our findings are not representative of social enterprises as a whole, even though this

program has included a diverse range of business models across numerous industries and at various stages of development. Future research needs to test our hypotheses with more generalized sample in order to secure external validity.

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