

# 1. European Enterprise Policy: Introduction

## Policy.

Market = Invisible hand (Adam Smith)  
↕  
Policy = Visible hand

**Policy** : to do something if the invisible hand fails.

Examples:

- Chalk: €0,10 → No policy needed
- Bread:€2 → Policy objective → reasonable price
- Why does education need policy → It's a basic need
- Plain Tbilisi – Gent → Should plains be public?  
Gent – Brussels → Public train (provided by government)
- Banks in trouble → Market failure: no regulation

Market works: regulation

Policy:

- 1<sup>st</sup> step: Identify that the market fails (show that market fails)
- 2<sup>nd</sup> step: Make market work (e.g. maximum price)
- 3<sup>rd</sup> step: Government/ Public sector takes over

## Enterprise.

Why do we need them? They create jobs, goods and services.

↳ only jobs through enterprises

Enterprise policy → where does the market fail?

- We need more enterprises to create jobs
- We need more growth and jobs
- Bankruptcy
- Delocalization (company moves because of lower costs) ↔ expansion

Enterprise policy:

- Policy start-ups
- Policy for growth
- Policy to avoid bankruptcy
- Policy to avoid delocalization

## European Enterprise Policy.

**Principle of subsidiarity**: every policy should be implemented on the lowest level possible.

↳ Condition: it has to be efficient

Access to finance → what level? European? National? Regional?



SME: 99% of all businesses in the EU

## 2. European Enterprise Policy: The dynamic role of SME's: Evidence from the EU experience.

SME= small and medium sized enterprises

### 1. Statements.

#### How dynamic are SME's?

"Small firms create more jobs than large firms. Mice, and especially gazelles, are more important for the maintenance and the creation of employment than elephants". (David Birch)

Conclusion from policy perspective: Be friendly with elephants (Phillips, Siemens, GM) and make them stay but focus on mice (start-ups) and gazelles. Elephants don't create new jobs, but are important to maintain.

#### SME's & growth

"The EU has a problem in start-ups but ever a bigger problem in scale-ups."

Share of highgrowth firms:

- (1) Turnover (omzet): US = 22% , EU = 11%
- (2) Employment: US = 7% , EU = 4%

#### The future of SME's.

Are SME's a necessary condition for the sustainable social-economical development of the new neighbors of the enlarged EU

### 2. Enterprise policy.

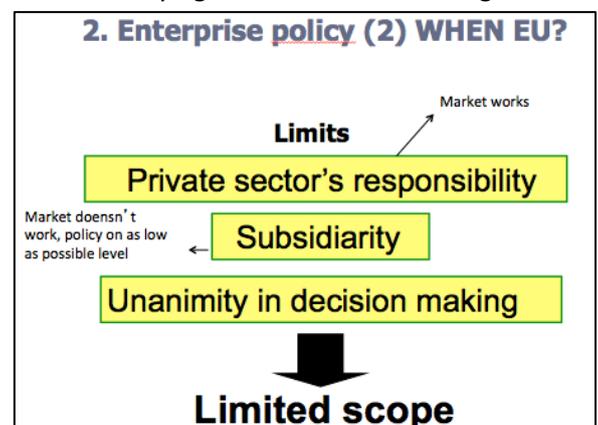
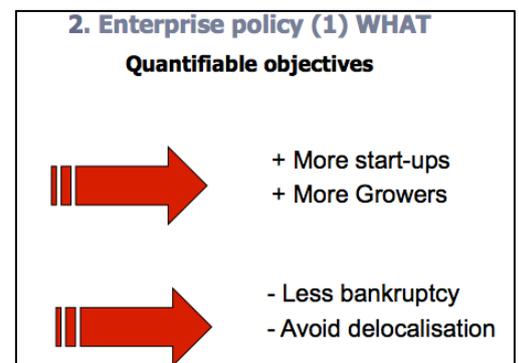
- **WHAT: The four objectives of enterprise policy**

| Objectives              | Policy                              |
|-------------------------|-------------------------------------|
| Create more enterprises | Start-up policy                     |
| Use growth potential    | Growth enablers policy              |
| Prevent Bankruptcy      | Bankruptcy and second chance policy |
| Avoid delocalisation    | Retention policy                    |

- **WHEN EU?**

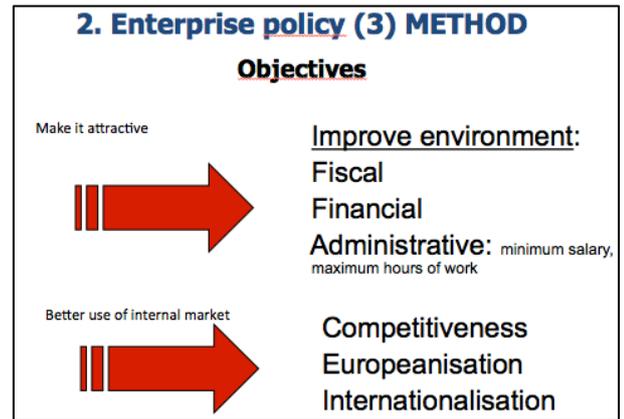
The best way to understand the European Union's role is to start identifying its **limits**. The following three principles of operations are relevant:

- **The private sector's responsibility**  
Priority should be given to the functioning of the market. (Government needs to make it work)
- **Subsidiarity**  
Market doesn't work, European enterprise policy has to be developed and implemented on an as low as possible level (What can be done in an efficient way at a lower regional level should not be done at European level)
- **Unanimity in decision making**  
In most of the fields relevant to enterprise policy, unanimity (unanimiteit) was the common rule. This often made it very hard to make decisions.



This set of principles leaves **limited scope** (beperkte mogelijkheden) for enterprise policy. The **objectives** of the enterprise policy at European level are two-folded:

- Increase competitiveness, the Europeanization and the internationalisation of enterprises.  
 ↳ *Make better use of internal market*
- Create a better administrative, fiscal and financial environment for enterprises.  
 ↳ *Make it attractive; Administrative: minimum salary, maximum hours of work.*



To achieve objectives: the Commission relies on different tools

- 1) Communications, recommendations and directives to the Member States
- 2) Exchange of experience, best practices and benchmarking (kwaliteitsbewaking) exercises
- 3) Pilot schemes which have a demonstrative effect
- 4) Direct financing schemes

### 3. From SME policy to entrepreneurship policy.

Three phases:

#### 1) Before 1980: Elephants (big is beautiful)

Elephants are a big companies that create jobs.

**How do we attract elephants (teaser)?**

- High-skilled, cheap labour
- Place (space)
- Logistics (ports, railroads)
- Booming market
- Investment subsidies
- 

Today all the elephants are leaving because none of the teasers are valid anymore.

→ **Delocalisation:** moving plants from one country to another for cost reasons

**Retention policy:** trying to avoid/postpone delocalization

- ↳ by tightening regional links with research centres, universities, incubators, policy makers
- ↳ subsidies are inefficient in the long run but postpone delocalization for some years
- ↳ elephants no longer create jobs, but are important to maintain them!

#### 2) 1980-2000: SME = Small and Medium Enterprises (small is beautiful)

**EVIDENCE BASED**

- **Major obstacles for development** → why don't SME's grow?
  - Finance: cost & lack of finance
  - Market: lack of own funds & lack of demand
  - Charges/Taxes: access to new market & fiscal and social charges

What should you (as state/country/Europe) do for more growth?

- Fiscal policy
- Market-policy → Internal market (cooperate with other companies)
- Export-policy → Promote export
- Innovation policy → ....

• **Gazelles**

fast growing enterprises → create lots of jobs.

Three major impediments (obstacles) to grow:

- Level of taxes and social security
- Red tape: bureaucracy of government administration
- Lack of capital (access to finance)

• **Constraints (beperkingen) of an SME policy:**

- Patchwork (lappendeken) of measures
- Lack of synergy
- Based on **subsidy policy** with contra productive effects:
  - o Too complex
  - o Too expensive/heavy application procedure
  - o Only few SMEs willing to accept support
  - o Creates discrimination amongst subs and non-subs.

With SME policy, **subsidy policy** you look at the wrong companies:

- Very good companies
  - o Most subsidies go to the lame ducks, this is bad, because sometimes very good companies get in trouble as well an don't get the help they need because the lame duck got the subsidies.
  - o Subsidies are a waste of money
    - Better use it to reduce level of taxes and social security
- Lame duck (survive but nearly don't make it)
- Very bad companies

**3) Entrepreneurship (2000 – 2010)**

Entrepreneurship is a mindset: a way of thinking.

↳ How can you measure it?:

**TEA:** Total entrepreneurial activity

- % of people that do go in the start-up
  - How many % of the people want to work for a start-up (more risk)
  - % of people that put money in start-up
- FFF: Friend, Family and Fools  
→ major financiers for start-ups.

→ Sum of these 3 = score on 100

|               | TEA 2012 |   |
|---------------|----------|---|
| Ierland       | 8,1      | The Netherlands<br>TEA = 10<br>Out of 100 people, there are 10 who<br>• Are working in a start-up<br>Or<br>• Go in a start-up<br>Or<br>• Put money in a start-up<br><br>In the Netherlands entrepreneurship is much more developed than in Belgium. |
| Griekenland   | 7        |   |
| Spanje        | 6        |   |
| UK            | 9        |   |
| Denemarken    | 5        |   |
| Duitsland     | 5        |   |
| Austria       | 10       |   |
| Zweden        | 6        |   |
| <b>België</b> | <b>5</b> |   |
| Nederland     | 10       |   |
| Italië        | 4        |   |
| Finland       | 6        |   |

### Move to entrepreneurship policy (EU)

- fostering entrepreneurship is a priority
- we claim we like entrepreneurship because ...
  - its impact on employment
  - its impact on growth
  - it fits into the “active welfare state”
- but entrepreneurship is not a characteristic of economic life (cf. USA)
  - entrepreneurship is a structural anomaly (afwijking)

### HORIZON 2020 → program 2014-2020

Targets:

3% innovation, 70% employment rate, 10% max level of school drop, 20 million less EU-poors  
20/20/20: less greenhouse gas emissions, target share renewable energy, more energy efficiency

Entrepreneurship can lead to:

- Personal wealth creation
- Bankruptcy

Attitudes:

In the USA successful entrepreneurs are regarded as heroes and those who have failed in their venture are granted a second chance, whereas in Europe bankruptcy laws almost totally prevent them from starting any new venture ever again, and those who are successful face discriminatory tax laws.

## 4. Conclusion.

In Europe is the focus no longer on SMEs, but they are still important, especially the gazelles.

Entrepreneurship policy instead of SME policy.

- Faster economic growth
- Create employment
- Improve competitiveness
- Promote regional development
- Focus on scale-ups

## 3. From SME policy to entrepreneurship policy.

### **A start-up package: as part of a single market strategy (sms)**

Uitleg internet:

SMS = European Commission's plan to unlock the full potential of the single market

SM (single market)

- people, services, goods & capital move freely
- opportunities for European businesses
- greater choice & lower prices for consumers

## 1. Evidence based policy

(basic philosophy of chief economist team)

There's a gap between policy and the evidence. → **Solution: Evidence Based Policy.**

Definition: 'policy making' based on:

- Systematic use of analytical data
- Analysis of the existing measures
- Ex-ante analysis of new measures
- General overview and synergy

**Evidence: why not to start up a business** (5 most important reasons from the Delta survey)

### 1) Financial risk

- Legislative (wetgevend) initiative on business insolvency (bankruptcy), including early restructuring and second chance (SMS)  
Vb European Network for Early Warning (from Cosme) gives support to enterprises & second starters
- can be limited by good **coaching** → some support programs:
  - *Startup Europe*: support services such as advice, networking & legal assistance
  - *The EC accelerator program*: time-limited support comprising programmed events and intensive mentoring, access to seed capital, angel financing, etc.

### 2) Lack of capital

**COSME** = EU programme for the Competitiveness of Enterprises and SMEs (from 2014 until 2020, budget: €2,3 bil)

- └ guarantees up to 80% of default risks: enabling new ventures to start operating
- └ 2 financial instruments facilitate access to loans and equity (eigen vermogen) finance for SMEs where market gaps have been identified

|   |
|---|
| Uitleg internet:<br>Default risks = exposure to loss due to non-payment by a borrower of a financial obligation |
|---|

### 3) Limited social security

- Access to unemployment allocations in case of failure:  
MS (member states) responsibility
- EC can stimulate **benchmarking**

#### **Benchmarking (kwaliteitsbewaking) exercise**

Aims to create the right environment for small businesses: removes obstacles to entrepreneurial activity & encourages success

##### 6 fields of intervention

education for an entrepreneurial society, training, access to finance, access to research and innovation, improved visibility of support services & better public administration

##### 5 steps

- *identification* of the problems
- *definition* of the main field in which projects should be developed
- *implementation* (in collaboration with MS)
- *adoption*: conclusions & recommendations are adopted + communicated
- *follow-up* (reports)

#### 4) Quality of life

Entrepreneurship is still an anomaly (not considered as the most normal option in life) in most European countries, such as France, Belgium, Spain and Germany. → TEA graph  
Becoming entrepreneur should become equal choice in life, not the 'last' choice  
→ Education is the key

#### 5) Don't see opportunities

1. SMS creates opportunities
2. COSME: stimulate entrepreneurship (to see opportunities)
3. SMS: make it easier to establish start-Ups in other EU country (simple VAT, legal certainty, EU-company law, trans-border financing)

### 2. Some evidences.

Employment policy does not create jobs, it is a target policy, focus on one group, policy works well for that group, employer wants people who have those criteria and wants people from the group to replace others → **Cannibalism**: macro-economic impact of employment policy is zero

*One can not love employment and hate enterprises and entrepreneurs*: Enterprise Policy doesn't care about enterprises but we love the employment they create.

Employment can be created by stimulating entrepreneurship.

**Entrepreneurship**: in Europe negative mindset

(start-up: in the past rarely considered as first choice of life)

**According to Plato**: if you do business; you go one year to jail, in case of recidivism (business after being in jail) 2 years.

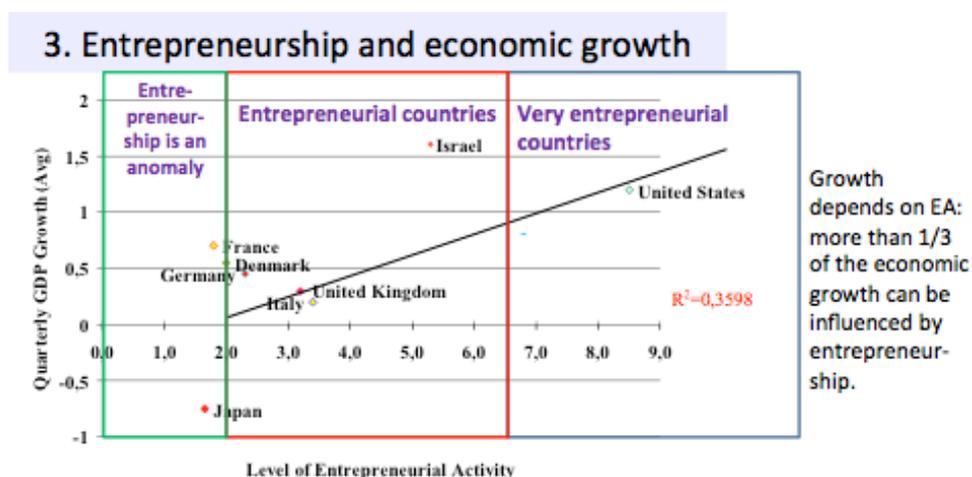
**Loi de dérogance**: noble people doing business would lose their titles

Failure is forbidden (Chinese proverb: failure is basis to success).

### 3. Entrepreneurship.

Entrepreneurship: measured by TEA index

- Positive correlation between TEA and economic growth ( $R^2=0,36$ )



#### **Correlation: year n and year n**

36% of the growth of the economy is determined by the level of entrepreneurship

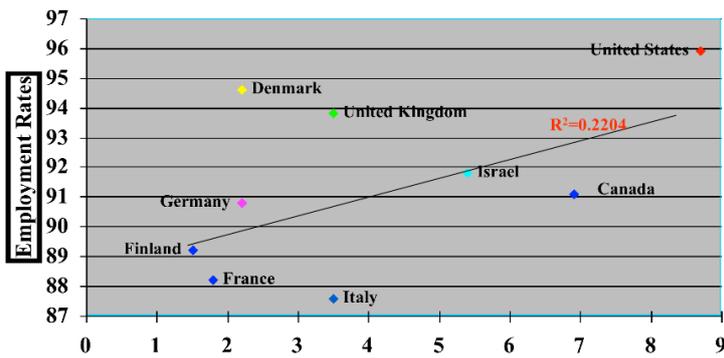
Best way to create economic growth is to stimulate entrepreneurship.

#### **Correlation: year n and year n+1:**

TEA of year n and correlate it of the year n+1, then you see that the correlation coefficient becomes 50.

Level of EA today will determine half of the growth of next year. Entrepreneurship is major determinant in economic growth.

- Positive correlation between TEA and employment ( $R^2=0,22$ )

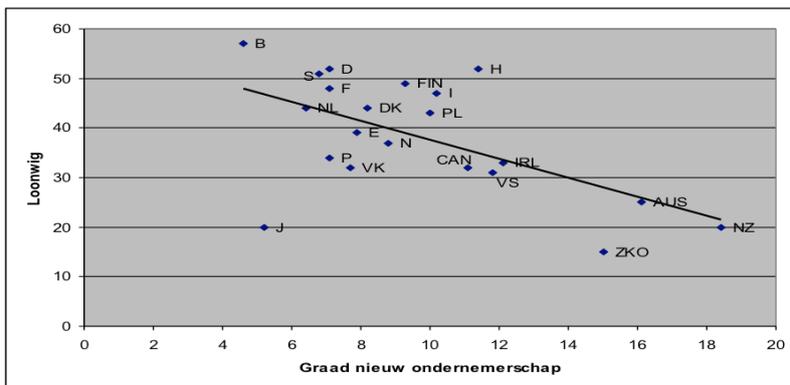


**Correlation**  
 22% of the employment level is determined by the entrepreneurship level.

Low level of entrepreneurship → low level of employment  
 High level of entrepreneurship → high level of employment

- Negative correlation between TEA and salary gap ( $R^2= -0,49$ )

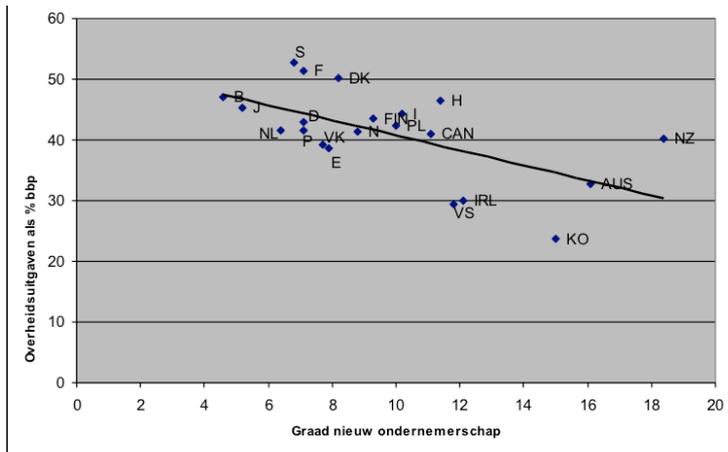
**Salary gap:** difference between gross and net salary. (BRUTO – NETTO = SALARY GAP)



High level of taxes → low level of entrepreneurship.

Japan, low level of entrepreneurship + low level of taxes.  
 Explanation: Entrepreneurship as people who work, do, invest in a start-up. In Japan, lot of people work in big companies (not a lot of start-ups)

- Negative correlation between TEA and public expenses ( $R^2 = -0,61$ )



**Entrepreneurship by opportunity:** Countries with high social security system

**Entrepreneurship by necessity:** Countries with low social security system (*there is no other choice, you do it to survive*)  
 → If a country is in crisis, people start businesses out of necessity.

Peru, country with the most entrepreneurship (by necessity).

#### 4. From SME policy to entrepreneurship policy.

##### Dynamics of entrepreneurship: business climate versus entrepreneurship climate

Future governments will orientate their policies and programmes more towards fostering entrepreneurship

| Business climate                         | Entrepreneurship climate      |
|--|-------------------------------|
| Macro-economic conditions                | Attitudes                     |
| Easy access to finance                   | Culture                       |
| Taxation issues                          | Failure and bankruptcy issues |
| Exploitation of the internal market      | Education                     |
| Employment and environmental legislation | Training                      |
| Administrative burden (last)             | Research and innovation       |

##### Constraints (beperkingen) of an SME policy:

- Patchwork (lappendeken) of measures
- Lack of synergy
- Based on **subsidy policy** with contra productive effects:
  - Too complex
  - Too expensive/heavy application procedure
  - Only few SMEs willing to except support
  - Creates discrimination amongst subs and non-subs.

##### SME policy:

- Helps SMEs to overcome obstacles
- Focused on enterprises
- Business environment (*we should create a context for companies*)

##### Entrepreneurship policy:

- Encourage people to think entrepreneurial
- Focused on entrepreneurs
- Entrepreneurial culture

| Policy       | SME  | Entrepreneurship                                   |
|--------------|--|--|
| Legitimizing | Market failure   | Lack of entrepreneurs                              |
| Objective    | To help SME's with their relative disadvantage (compared to big E) | Be undertaking (start a business, grow, mentality) |
| Target       | businesses   | entrepreneurs                                      |
| Levers       | Financial (subs.)  | Mainly non financial                               |
| Focus on     | Business environ.  | Entrepr. culture                                   |

#### 5. The main actors.

Entrepreneurship is a mindset blending creativity and risk-taking with sound management.

##### **A. Individuals:**

To consider entrepreneurship as a career option

##### **B. Firms:**

To adapt change for survival and seize new opportunities

To organize the business to exploit human capital

##### **C. Society:**

To provide a supportive environment, where entrepreneurial initiative and risk-taking is appreciated

To value the contribution of enterprise to society

#### A) The individual as a prospective entrepreneur:

*SME: A business environment conducive (bevorderlijk) to start-up.*

- Barrier to entry market      *Why don't you start-up?*
- Access to seed finance      *Money for initial capital to start a business*
- Support – incubator      *Helps start-up become succesful*

*ENT: Fostering an entrepreneurial culture:*

- Motivation: labor market, tax and social charges, attitudes to risk and failures, target groups
- Education and skills

#### B) Firms as drivers for growth and competitiveness.

*SME: A business environment conducive to thrive and survive.*

- Red tape (excessive bureaucracy), restructuring, the Internal market
- Resources: skilled labor and finance

*ENT: Fostering an entrepreneurial culture:*

- Motivation: ambition to internationalize and grow, taxation
- Capacity: adapt to value innovation, intrapreneurship

#### C) An entrepreneurial society.

*SME: Contribution of society to entrepreneurs:*

- Appreciation of entrepreneurship by teachers, investors, family and friends
- Reward risk and tolerate failure

*ENT: The contribution of entrepreneurs to society:*

- Responsible entrepreneurship
- Social economy and social enterprise

### **Entrepreneurship and innovation: the territorial approach**

Entrepreneurship → mindset → innovation (can be disruptive, allowing small players to challenge major ones)

From status culture to project culture: we need to move toward risk-taking and learning from failure

→ Repositioning of public action is necessary: Four priority lines of action:

1. A common vision at the relevant territorial level
2. Ensure active involvement of residents
3. Create an adequate legal and fiscal framework
4. Encourage the development of radical innovation

### **6. Policy implications and benchmarking.**

#### **The role of policy makers:**

- An holistic approach to entrepreneurship policy is needed, to take into consideration that entrepreneurship determinants cover such a wide range of issues
- Actions are needed at European, national and local level

#### **The role of the European Commission:**

- Setting the agenda: identifying policy topics for action
- Defining the needs: developing measures for entrepreneurship
- Addressing availability of comparable data
- Monitoring progress and benchmarking.

## 4. CASE: Measuring entrepreneurship: Entrepreneurship in Netherlands vs Belgium

### 1) Importance of third factor: entrepreneurship, innovation and creativity

The 2 determinants of growth → Cobb-Douglas: Productivity

Growth = f (C,L)                      C (capital) & L (labour)

$$Y = aL^\sigma + bK^\beta \quad Y \text{ (productivity)}$$

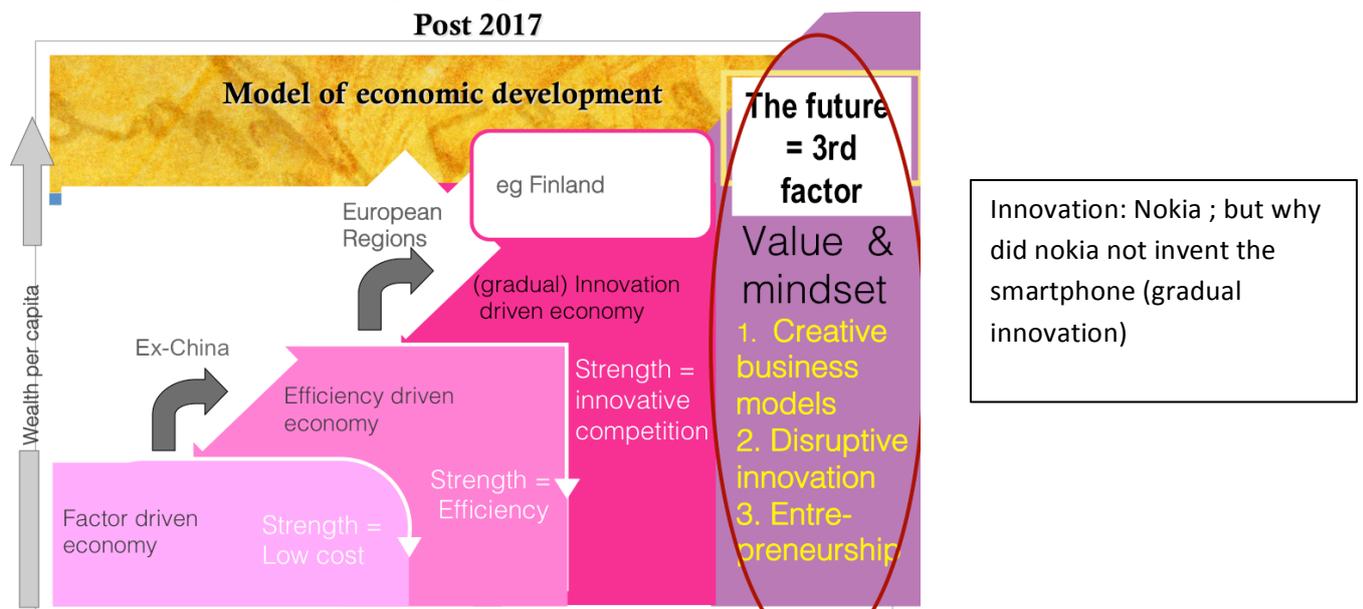
→ The end of a model:  $Y \neq f(C,L)$

- A lot of labor (unemployment)
- A lot of capital (interest close to zero)
- But growth remains relatively low
- Cobb-Douglas doesn't work anymore

Model of economic development

The third factor:  $Y = (\text{Creativity, Innovation, Entrepreneurship})$

- **Intangible factor** (niet tastbaar) but powerful!!!!
- Studies: **determines 2/3 of economic growth.**
- Measured through **GEM** (global entrepreneurship monitor)



### Creative business models

A new world: Blockchain (gemeenschappelijk databeheer) & digitalisation: this is the end of the middle-man & the fee business

→ Almost all unicorns are creative business models

|                                     |  |
|-------------------------------------|--|
| <b>1. The advertising model</b>     | Google: 90% is publicity   |
| <b>2. The free-rider model</b>      | booking.com: biggest hotel revenues without hotel-infrastructure (idem Uber)   |
| <b>3. Circural model</b>            | Mobypark: private parking renting  |
| <b>4. The Freemium model</b>        | Spotify (free against data)  |
| <b>5. The reverse pricing model</b> | Kopenhagen Fitness: consumer establishes his requirements and offers those requirements for bid by the seller → sellers have to compete for their business |

**Entrepreneurship is a mindset**

Cartoon: Resistance to change

*“This really is an innovative approach, but I’m afraid we can’t consider it. It’s never been done before.”*

**Schumpeter (1917): creative destruction**

= proces van voortdurende innovatie waarbij succesvolle toepassingen van nieuwe technieken de oude vernietigen → technologische innovatie = enige echte bron van economische groei  
 Nokia “vernietigd” door innovators (bv Apple), ze waren te veel op hun gemak

Entrepreneurs: those who understand that there is little difference between obstacle and opportunity, and are able to turn both to their advantage

Mindset

**1. Individuals**

- to consider entrepreneurship as a career option

**2. Firms**

- prefer growth over control
- ‘big boss, small company syndrome’

**3. Society**

- to provide a supportive environment, where entrepreneurial initiative and risk-taking is appreciated
- to value the contribution of enterprise to society

2) Netherlands compared to Belgium

**GEM on 62 countries:  
10 criteria: Be – NL: 2 - 8**

|                                  | BE | NL |   | BE | NL |
|----------------------------------|----|----|---|----|----|
| Percieved opportunities          | 36 | 22 | Female/male opp                           | 60 | 1  |
| Percieved capacities             | 54 | 47 | Innovation                                | 36 | 44 |
| Pos fear of failure              | 58 | 21 | Status of entrepreneurs                   | 46 | 36 |
| Pos attitude to entrepreneurship | 44 | 47 | Entrepreneurship as a good choice of life | 38 | 2  |
| Female/male motivation index     | 38 | 8  | EEA: entrepreneurial employee activities  | 12 | 10 |

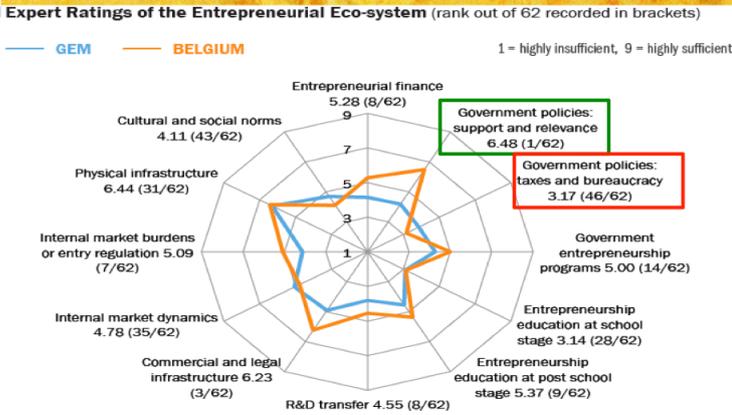
**Rankings .....**

|                               | BE | NL | Total n° of countries |
|-------------------------------|----|----|-----------------------|
| World bank: doing business    | 43 | 26 | 189                   |
| World bank: starting business | 20 | 18 | 189                   |
| WEF: competitiveness index    | 19 | 5  | 140                   |
| Tax compliance cost           | 8  | 5  | 32                    |
| Glass ceiling index           | 8  | 24 | 27                    |

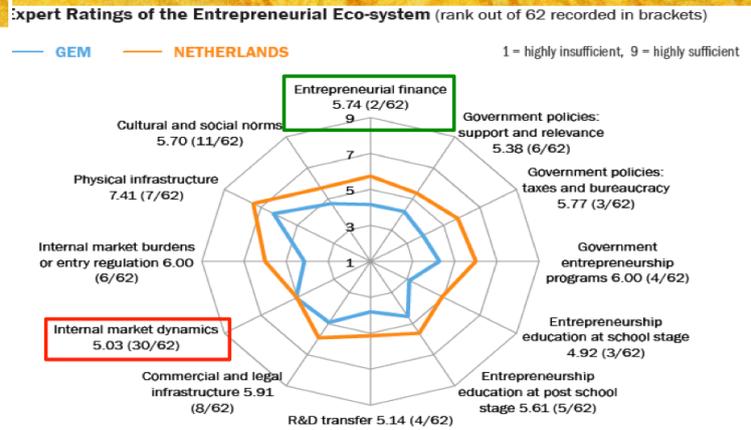
→ Start your business in the Netherlands, do business in het Netherlands and be competetive but glass ceiling: if you’re a women, don’t work in the Netherlands. (Netherlands level of Turkeye)

SWOT analyses

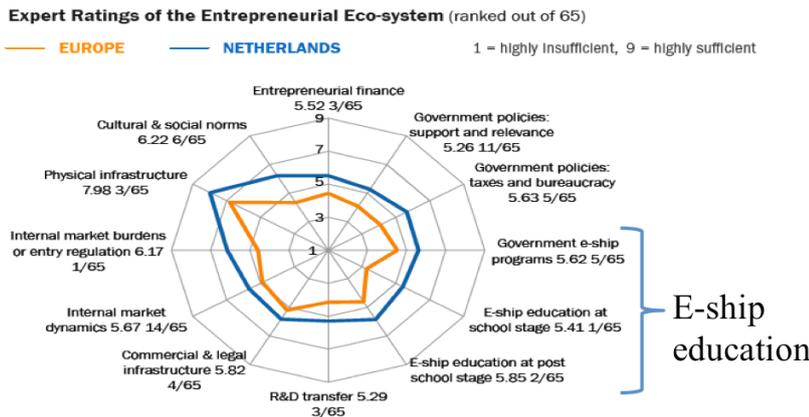
BELGIUM : SWOT analysis



Netherlands: SWOT analysis



Netherlands : the best in e-ship education



5. ESCALAR: A SBIC for Europe?

Increase efficiency of government efforts in finding ways on how guarantees can be used to facilitate access to venture capital (VC).

Guarantees: formal assurance that certain conditions will be fulfilled

Venture capital: capital invested in a project in which there is a substantial element of risk.

1. The US SBIC

Equity = eigen vermogen ( activa – schulden)

SBIC = small business investment company

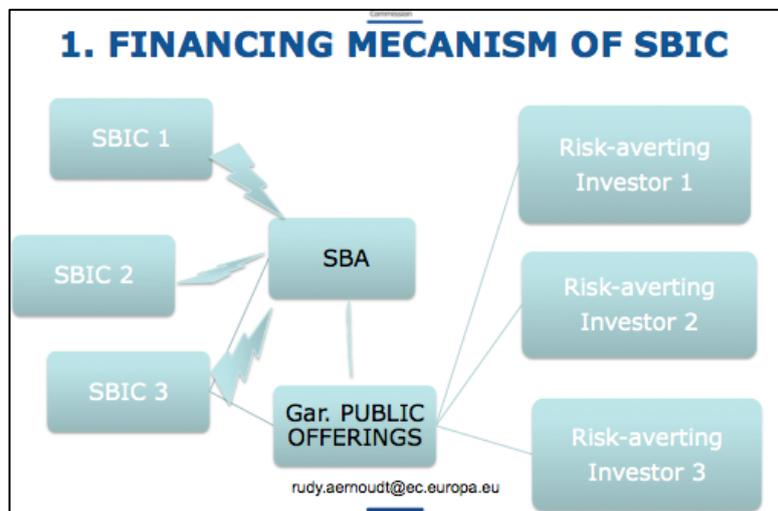
Privately owned and managed investment firms that use their own capital, plus funds, obtained at favourable rates with an SBA guarantee, to provide loans and venture capital investments to small businesses. Virtually all SBICs = profit-motivated businesses

- Aims to increase availability of longterm equity and loan financing to SMEs
- Main & only programme of support for venture capital at US federal level
- At zero budget cost (cost to the taxpayer is negative; programme pays for itself)



Most SBICs are owned by relatively small groups of local investors, however many are owned by commercial banks

**SBA** = small business administration → licences & regulates SBICs  
 The SBA never buys SBIC securities itself – it only guarantees them



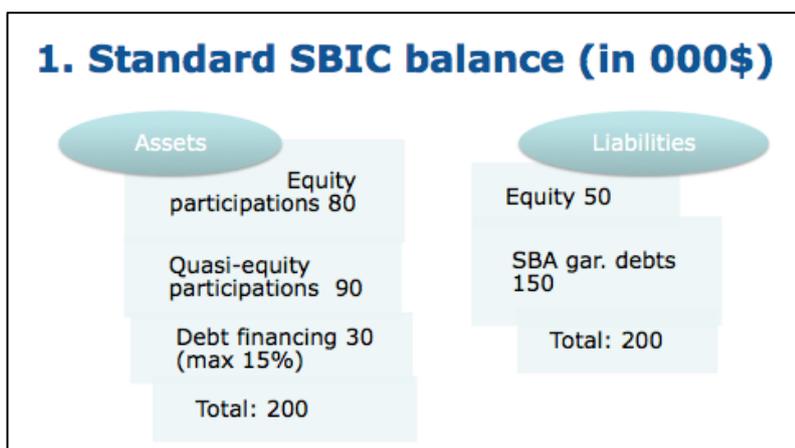
|  |   |
|--|---|
| Leverage   | 2 to 3 non-guaranteed equity  |
| Equity cap   | Min. M\$ 20; max M\$ 75   |
| Debt conditions                                    | 10 yr treasury + 0,5 to 2,5% (eg in September 2016 4,7%)  |
| SBA fees (are adapted to make SBIC at 'zero cost') | Usage charge 0,35% (2017)<br>Leverage fee: 3%;<br>License fee: min 25 000\$<br>Examination fee: 4000 to 14000\$ |
| Investees  | SMEs  |
| Instruments  | Equity/quasi/debts (max. 15%)   |

Basic advantage of the system = **leverage**

= funding which SBICs can raise on public capital markets by using an SBA guarantee or by selling securities directly to the SBA.

Obtaining leverage:

- 1) regular SBICs sell debentures (debt securities) or participating (equity-type) securities guaranteed by the SBA
  - 2) Pools are formed, and SBA-guaranteed participation certificates are sold to investors through a public offering.
- a SBIC may leverage up to 300% of its private capital!



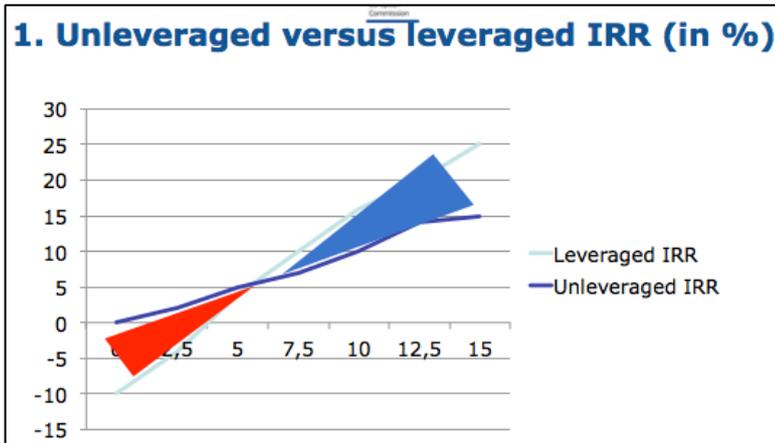
Gar. Public offerings are offered to risk averting investors → SCHULD (DEBT)

With which the SBIC finances debt from SMEs → VORDERING

| 1. SBIC Licensing Process  |  |  |
|--|--|--|
| Initial review   | Raise Capital  | Licensing  |
| <b>Management Assessment Questionnaire</b><br>Applicant submits application with <ul style="list-style-type: none"> <li>▪ fund strategy.</li> <li>▪ track record.</li> <li>▪ Investment committee</li> </ul> | <b>Proof of capital</b><br>Applicant must raise <ul style="list-style-type: none"> <li>▪ \$20 million minimum before guarantee application.</li> <li>▪ sufficient capital to execute BP</li> </ul> | <b>Due diligence.</b> <ul style="list-style-type: none"> <li>▪ legal review.</li> <li>▪ FBI background check.</li> <li>▪ division and agency review</li> <li>▪ Administrator review</li> </ul> |

Eligibility conditions:

- Experienced team of fund managers
- A realized track record of investment return
- Evidence of strong deal flow in the proposed investment area;
- Limited management fee (1% to 2,5% max)
- Managerial, operational and/or technical experience
- A demonstrated ability to manage cash flows in order to assure that the SBA will be repaid.



**Effect of leverage** is to **reduce the average cost of capital** for the SBICs investment programme:

Equity returns are **geared upwards** if the company's investment portfolio makes a return above the interest cost

Equity returns are **geared downwards** if portfolio does poorly

**IRR:** internal rate of return

## 2. ESCALAR

There's a big gap between the European and American venture capital market, European venture capital markets are too thin → Escalar: a SBIC for Europe?

**ESCALAR = European Scale-up Action for Risk Capital**

→ Missing link to the scale-up gap: helps small businesses scale-up (expand, become bigger)

- 1) Scale-up & equity gap
- 2) Banking sector fragilized (post crisis)
- 3) Very liquid market – patient investors looking for AAA investments (Basle III)
- 4) Pan-European FoF operational
- 5) Already very public market (40% of EU VC is public); crowding-out danger

## 3. Implementation issues

Management:

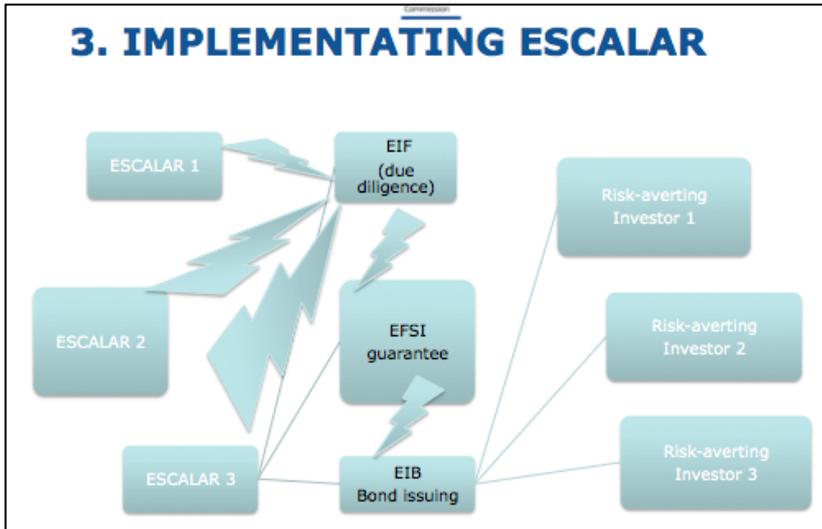
- Conception & policy coordination: GROW/ECFIN
- Due diligence (examination/licensing/call): **EIF** (European Investment Fund) = 'gepaste zorgvuldigheid'
- Management Bond issuing: **EIB**

Target VCs (venture capital):

- Investment phase: focus on scale-up; later stage?
- Co-financing: blending possible? (with national and European co-investment schemes)

Budget & legal issues

- Guarantee: **EFSI** (European Fund for Strategic Investments)  
→ helps overcome investment gap
- Working costs
- Fees (revenues)



Escalars are examined by EIF  
 Guarantees are given by EFSI  
 Bonds are issued by EIB to investors

**CCCTB = Common Consolidated Corporate Tax Base**

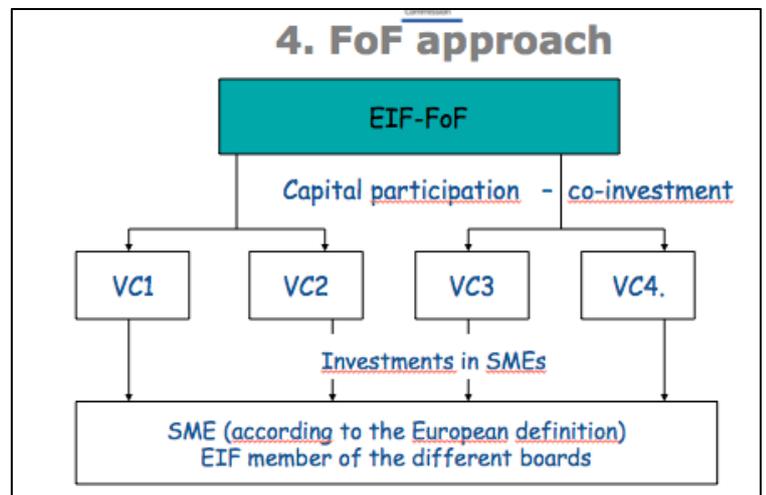
→ proposes to support small and innovative companies that want to expand their business across borders (taxation simplifications)

4. Complementarity with FoF

FOF = fund of funds

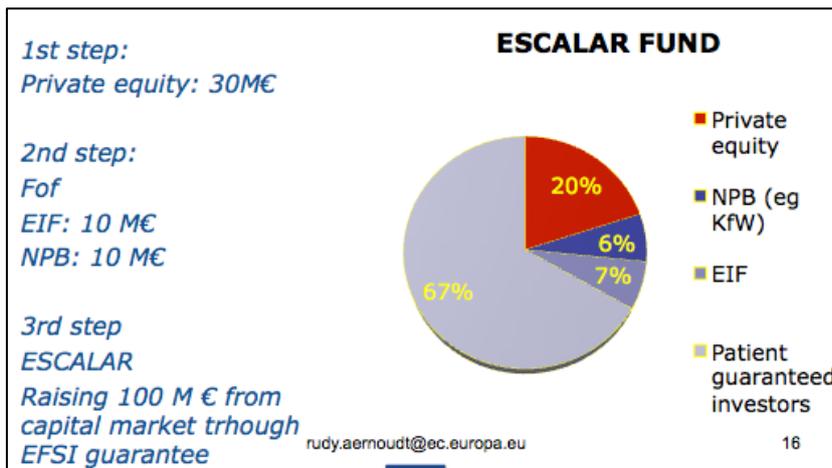
Wikipedia:

A **fund of venture capital funds** is a fund of funds that invests in a portfolio of different venture capital funds for access to private capital markets (facilitate access to finance to SMEs)



| Complementarity of FoF to SBIC                             |   |                                  |
|--|---|----------------------------------|
|  | FoF   | ESCALAR                          |
| Senior position (hogere positie) towards private investors | No: pari passu (gelijke positie)                                | Yes, senior (reverse pari passu) |
| Involvement of officials in management of funds            | Yes, board positions  | No intrusive governance          |
| Cost of program  | Depends on exits  | 'zero cost'                      |
| Costs for VC funds   | No, free lunch  | Yes, high fees                   |
| Advantage for private investors                            | Co-investment, No leverage on return; Hard to attract int. inv. | Leverage on return               |

5. Blending of financial instruments



NPB: national promotional banks

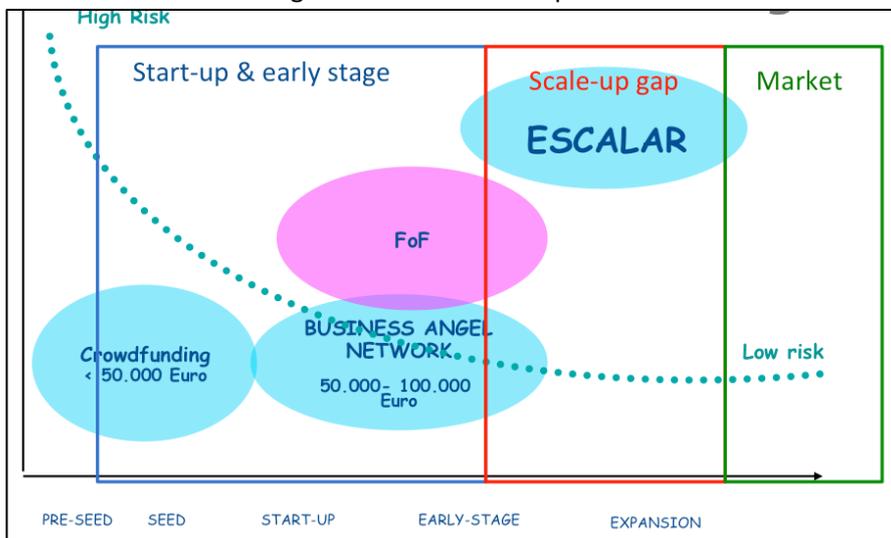
6. Stakeholders

**Five winners, no losers!**

- Taxpayer (pays zero)
- Scale-ups
- Employment → closing scale-up gap creates more jobs
- Patient investors (alternative invest)
- Equity investors (equity kicker)

7. Conclusion

ESCALAR is the missing link → boost scale-ups



## 6. Growth & Gazelle.

What makes a company grow?.

- Innovation
- Profit (to finance growth)
- Productivity
- Environment (reason why companies export to other more grow-supportive markets)

Growth is an issue for all types of companies.

- *I am a Fortune 500 CEO under pressure from Wall Street to grow my business and grow it faster. This means heavy short term investments, which put pressure on short term results.*
- *I've got a small (medium) size business that's been around for a decade and it is still small. It's not growing. How do I break through?*
- *We're a start-up. We are cashing on our passion but... How do we design a business that is born to grow from the start?*
- *I've put years into my business... blood, sweat and tears. Now it's time for my business to give something back to me. But it won't grow. Now what?*

**Entrepreneurial behavior:** study of the Top100 companies on the New York Stock Exchange (NYSE).  
*What do all these companies have in common? How do some companies go from zero to success in no time? What is the DNA of a company? Is there a blueprint? ....*

What makes the difference?:

- Attitude
- Perseverance
- Giving up is for the competition

The blueprint companies were all strong on the fundamentals (Apple, Priceline, ...):

- Think customer (*which type of person is interested in which type of product?*).
- Exceptional people (*people with innovative idea and who tend to keep working on this idea, because they want to pursue their dreams; Joe Average will never become a star*).
- Game changing strategy
- Superior execution (*quality*)
- Cash flow positive

### **10 Multipliers of exponential business growth:**

#### 1. Unleash the entrepreneur

*From the CEO as steward to the CEO as entrepreneur*

Create your business vs. run your business.

*Jobs created entirely new businesses: user-friendly PC, iPod, iTunes, iPhone, iPad, ...*

#### 2. Change the game with disruptive innovation

Start with focusing on the customer's frustration with your industry, company, offerings, ...

*Streaming video (Netflix) vs. video stores (Videoland).*

Innovation starts with leveraging what you have always done well in a new context

*Late opening hours by banks for the people who work late.*

3. **Target a high growth market segment.**  
 Moving from high-end to low-end  
 Moving from low-end to high-end (from coffee-shop to Starbucks).
4. **Come up with a breakthrough value proposition.**  
 Focus on the jobs that people want done & combine it with low price  
 Vb distribution of software with pay-per-use model
5. **Design thinking an rapid prototypes.**  
 Vb beta software, free downloads
  - Observe customers and see unarticulated needs and unmet wants
  - Create a quick prototype and get it into customer's hands
  - Get feedback and iteration
  - *The customer doesn't want to buy a drill, they want a ¼ inch hole.*
6. **Break into new markets with "Godfather" partnerships, Marquee Customers.**  
 What goals do you want to reach faster and what are the partnerships you can create to reach them the fastest?
7. **Make your marketing revolutionary and the competition irrelevant.**

| RED OCEAN STRATEGY   | BLUE OCEAN STRATEGY   |
|--|---|
| compete in existing market space   | create uncontested market space   |
| beat competition   | make competition irrelevant   |
| exploit existing demand  | create and capture new demand   |
| make the value-cost trade-off  | break the value-cost trade-off  |
| align whole system of company's activities with strategic choice between differentiation or low cost | align whole system of the company's activities in pursuit of differentiation and low cost |

8. **Grow your business on the web.**  
 Build a personal brand through social media that helps sell your product or service.  
 The three C's:
  - Content: blog to be seen as an expert
  - Community: have a social media strategy
  - Commerce: use innovative e-commerce tools
 Get your customers to sell for you: use what you sell, sell what you use.  
*Customers don't want to talk to a vendor, they want to talk to each other. Deliver great customer experience, and create a forum for people to talk to you and each other.*
9. **Drive growth through operational excellence.**  
 Get cash flow positive, minimize debt, be frugal (retain cash), have fun.
10. **Be a multiplier not a diminisher.**  
 It is all about unleashing what people already have inside them that is maybe suppressed in most work environments. Win over the spirits of the employees.

### **Create more companies:**

Based on simple math, this means:

- more potential of high-growth companies
- more potential of wealth
- recent US presidential campaign

Presence of companies creates more companies, creates more opportunities, creates more jobs, creates more wealth, creates more companies.



### **Finance growth:**

- Auto-financing is often/always not sufficient *Finance your growth, otherwise no growth*
- Internal restructuring
- PPS (Public Private Structure) *Singapore*
  - o 25% EIB (should be more active)
  - o 25% Private investor
  - o 50% Pension funds & insurance companies
- SBIC model US
- Convertible bond (long term-vision) (*loan, if I can't pay back loan you become share-holder*)
- Industrial vs. financial partner

### **Remove barriers:**

- Difficulty accessing financing
- Excessive administration regulation
- Excessive taxation – keeps existing companies from becoming high-growth companies
- More co-operative syndicates (no Belgian-type labor-unions) – employer is no criminal
- Reliable (national) infrastructure (transport, logistics, communication)

*Make it easy for companies to grow. Make it easy for companies to hire people.*

**Growth potential: local vs. international & growth support:    **GO BIG!****

#### **Local vs. international:**

- Cost of Sales & Marketing
- Fitting employees
  - o Skills
  - o Cost
  - o Flexibility
- Taxes & access to capital
- Size of Customers
- **Partnerships**
- Operating cost
- Stable political climate

#### **Growth: main obstacles**

- Labor costs
- Taxations
- Financing (cost, access, lack of own capital)

### **Growth support:**

- Big market size (large customers)
- Employee – attractive
  - Buying power
  - Universities – cheap labor
  - High flexibility
- Low taxes (special start-up)
- Island vs. stimulating biotope
- Low operating cost
- No strikes
- Mobility
- Social Security = rewarding job

### **Focus on universities and immigrants:**

Immigrants who plan to start businesses, not those who turn the social security system in bankruptcy.

Assist universities in R&D for the industry (MIT)

- Encouraging innovation
- Removing barriers to commercialization of university research
- Financial agreements/sponsorship
- Go-to-market driven research
- **Get bright minds from somewhere else and put them together.**

### **CONCLUSION:**

To build a biotope for fast growers and gazelle companies is the effort of a community, where each group and function has its specific responsibilities (public, private)

Creating jobs is not an obligation but a consequence of a motivational and stimulating environment.

Entrepreneurs striving for fast growth, having the ambition to build “gazelle companies” create, as a consequence, jobs and wealth.

## **7. Policy attitudes towards equity issues.**

### **Financing:**

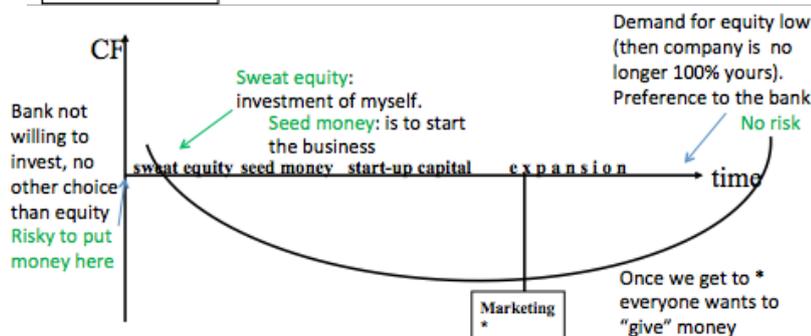
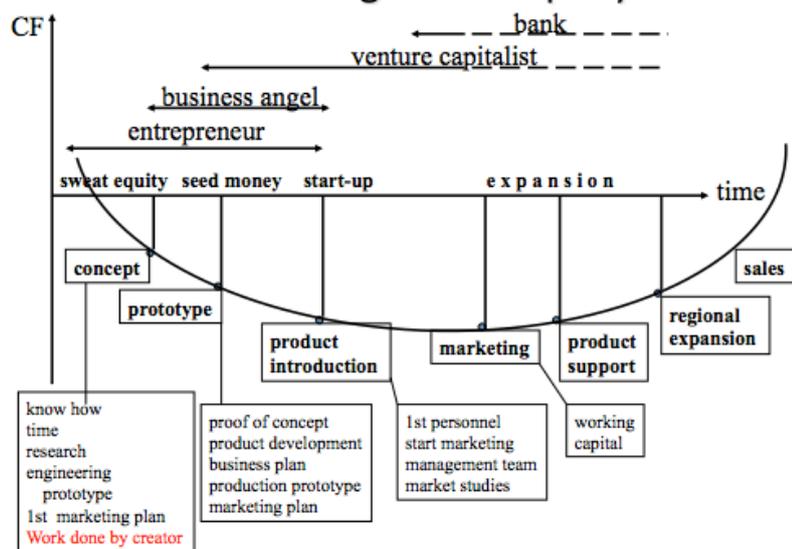
- Debt financing = loan/credit (you have to pay back) (banks)
- Equity financing = **venture capital** → share of the capital → one who gives equity is shareholder

# 1. Some evidences.

## A. Not all the money is the same.

|                                    | Pros  | Cons  |
|------------------------------------|---|---|
| <b>Friends, family &amp; fools</b> | <ul style="list-style-type: none"> <li>- easy to get</li> <li>- patient</li> </ul>                                      | <ul style="list-style-type: none"> <li>- limited added value</li> <li>- no deep pockets</li> </ul>  |
| <b>Public sources</b>              | <ul style="list-style-type: none"> <li>- free</li> <li>- patient</li> </ul>   | <ul style="list-style-type: none"> <li>- bureaucratic</li> <li>- slow, hard to locate</li> </ul>  |
| <b>Banks</b>                       | <ul style="list-style-type: none"> <li>- potentially cheap</li> <li>- relatively fast</li> </ul>                        | <ul style="list-style-type: none"> <li>- unpredictable</li> <li>- require security, impatient</li> </ul>  |
| <b>Business angels</b>             | <ul style="list-style-type: none"> <li>- fast, unbureaucratic</li> <li>- business understanding</li> </ul>              | <ul style="list-style-type: none"> <li>- no deep pockets</li> <li>- often unsystematised</li> </ul>   |
| <b>Private equity</b>              | <ul style="list-style-type: none"> <li>- deep pockets</li> <li>- value added easy to ascertain, clear agenda</li> </ul> | <ul style="list-style-type: none"> <li>- potentially unpredictable agenda, potentially slow</li> <li>- high expectations</li> <li>- difficult to get</li> </ul> |

### Financing of a company



If you do something in the field of policy, what do you need to prove?  
 Prove that the market fails, companies with good perspective do not find the money  
 In what case should we not need a policy?  
 If company gets money it needs  
 Risky to put money in early stage.  
 When will a bank be willing to give money? As soon as you start making profit

In the beginning starter will want to go to the bank, but the bank is not willing to invest. (Profits are too far away). Starter will have to ask for equity.  
 Demand for equity is high in the beginning. } Supply doesn't match demand = **Market failure**  
 Supply of equity is high in the end

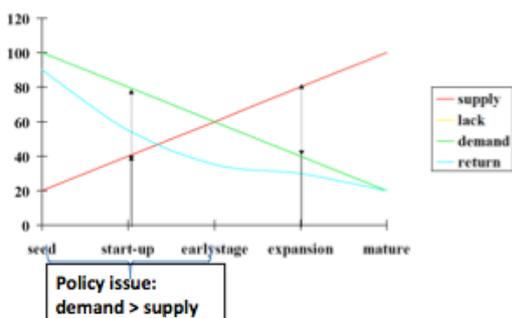
## B. The market does not function at the lower end

### Two issues that show that the market doesn't work:

- **Demand issue**
  - Entrepreneurs prefer control over growth
  - Only 7% accept to open their capital for external money
- Information asymmetry
  
- **Supply issue**
  - Risk/return: example of market imperfection
  - Lack of professionalism
- Inverse risk premium

### Evidence II: Market does not function at lower end

Supply/Demand and return for risk capital by development stage



#### Seed-phase:

- Supply of equity will be very low
- Demand of equity is very high

**Mature-phase:** Everybody tries to avoid equity and take the bank. Equity-supply is high.

#### Start-up-phase:

- Supply of equity low
- Demand of equity high

What is difference between demand and supply? **Market failure.**

Companies that want to get started, but cannot because they can't find the money they need = measurement of market failure.

Lot of companies don't get started because lack of money = policy issue

**Expansion-phase:** more supply than demand

No market failure because every enterprise that wants equity can find it

**Blue line:** return wanted by equity-player (doesn't ask interest, has shares)

Why difference in return between seed (80) and mature (20)? Because of the high risk

**Second market failure:** if you find the money, you don't find it at reasonable cost

## C. Negative risk premium

Point of view from the investors

|           | Development stage (Ontwikkelingsfase) | 1 year | 3 year | 5 year | Return Gecumuleerde IRR |
|-----------|---------------------------------------|--------|--------|--------|-------------------------|
| High risk | Early stage                           | -13,3  | 11,8   | 12,4   | 9,6                     |
|           | Expansion stage                       | 9,8    | 16,7   | 17,7   | 12,4                    |
|           | Totaal risicokapitaal                 | -5,4   | 16,7   | 20,2   | 12,0                    |
|           | Buyouts                               | 1,3    | 20,8   | 16,3   | 15,3                    |
|           | Totaal private equity                 | -4,5   | 19,1   | 17     | 12,9                    |

Normal market:

- High risk → high return

This market: inverted market

- High risk → low return
- Low risk → high return

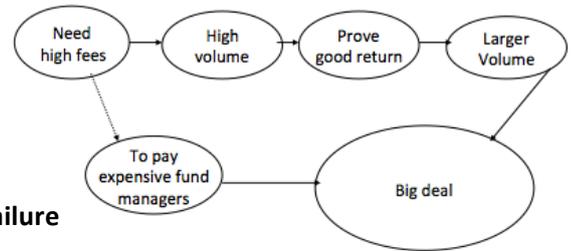
What can we do from the policy point of view?

#### D. There is a natural tendency for big deals.

Nobody wants to invest in small amounts (small money).

The average seed investment : 1.1 million €

When you need a small amount, there's no money = **market failure**



#### 2. European facts and figures.

Every year 1.6 million enterprises are created. 150 000 want to grow (are growth oriented) and they offer a sufficient, but not extra-ordinary return for investors. 3000 get venture capital.

→ **Market failure:** 147 000 enterprises do not grow, do not get launched, because they don't find the money. (2 out of 1000 starters gets venture capital in EU).

This is the proof that equity is an issue!

Why should we care? **Employment!** 5% of companies creates 80% of employment.

10 000 good technological business ideas



1000 get created



100 get venture capital



10 go public (to stock market)



2 become market leaders (gazelles)

Why should we not only concentrate on the 2 gazelles? Why the others?

How do you know who will make it to the end?

#### 3. Governments' role.

Desired government actions for financing: What do entrepreneurs want from the government?:

- **Stimulating self-financing in a fiscal way** (*Problem? debt by bank → interest = costs, you can deduct them from your profits = less taxes; Financing with equity ≠ debt, no interest, no cost, more taxes → People avoid taxes, and therefore we prefer to finance with debt. Companies want a chance to put their money in their company, and give us a fiscal advantage → Notional interest*)
- Reinforcement of interest subsidy
- Diminishing of bank coalitions (*make market of the banks work*)
- Reinforcement of government guarantees
- Foundation of a SME investment fund (*small amounts at the beginning*)

#### Supply side:

- All instruments integrated within one organisation = One-stop shop for SME financing
- Integrated finance approach

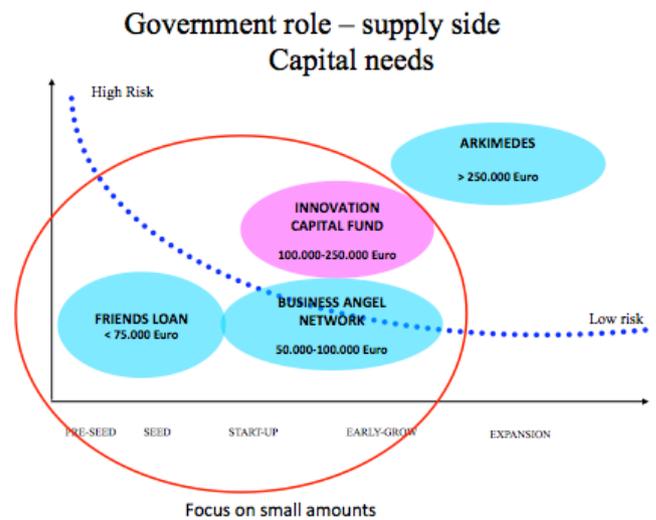
#### European initiatives:

- ETF start-up
  - Fund of funds principle
  - Start-up or expansion phase
- SEED
  - Working costs for seed funds

- Guaranteeing guarantee schemes
  - Co- or counterguarantee system

### Capital needs:

- **Friend-loan (Aunt Agaathe):**
  - someone loans you €10 000, in case you go bankrupt; 30% is paid back by the government and each year he gets a fiscal privilege.
  - Linking money and affection
  - Fixed incentives for direct investments
- **Business Angel Network.**
  - Merger of network
  - Performance criteria (milestones)
- **Innovation Capital Fund**
  - Spinoffs/spinouts/2<sup>nd</sup> round (focus)
  - EU cofinancing will be sought
- **ARKImedes (SBIC – inspired)**
  - principle levy on private money
  - capital guaranteed by the government:
    - 90% on shares//100% on bonds
  - with tax incentive :35% tax reduction on shares
  - money to be invested together with private VC money (50/50 basis)
- **Modernizing guarantee systems**
  - portfolio approach
  - no involvement on project level
  - EU backed system for starters: 75% guarantee & 50/50 base with EU
  - Bench: German and Dutch scheme



### Demand side:

- Investor readiness: try to educate to educate entrepreneurs in order to make them open to capital.
- Integrated finance approach: *go to bank → refuses, go to public → refuses, go to equity → difficult*; instead of going to each of the above, you can go to a panel who say what sort of finance suits your idea. (fit4finance)
- Stimulate entrepreneurship
- Casebook of venture capital backed companies

### Demand meeting supply:

- Mutual Understanding between bankers and SME's
- Business angels academy
- Creating platforms
  - Belgian venture capital summit
  - Financial breakfasts
  - Yearly financial symposium

#### 4. Conclusion.

- Need for more entrepreneurial finance
  - Need for more real entrepreneurs
  - Need for stimulating government measures
- ➔ Only then will more venture capital backed companies grow, leading to economic growth and employment.
- 

## 8. Business angels and their networks.

Business Angel (= person, not a fund)

People with:

- Money
- Experience in enterprises
- Time

1,1 – 1,3 million people possess those 3 criteria

- 100 000 invest → **Active Business Angel**
- 1-1,2 million don't → **Virgin Business Angel**

Policy objective: get more people to invest.

We can't invest in BA, because they already have a lot of money.

**What do BA want? Or why don't they invest?.**

- Where find projects? How?
- People with money, no ideas (potential BA)
- People with no money, good ideas (potential start-up)

How can we match them → **Business Angel Network**

- Makes database with all the projects
- Makes database with all business angels

**MATCHING PRINCIPLE** → Way to contract the other

Why does European Commission give subsidies directly to BAN and why does it have to go through EIF to invest in VCF?

Same market failure, solution in VCF and supplementary solution in BAN.

### Two market failures:

Market failure 1: you don't find money for start-ups. Starting companies, because the risk is very high and risk is not rewarded by return → investors don't invest in start-up.

Market failure 2: everybody wants to invest big amounts (big deals), people looking for small amounts can't find them.

→ A lot of ideas do not lead to start-ups. Lot of ideas are lost. We could have more start-ups if every good project would find his financing.

**Objective in policy**: every start-up should find money.

*invest in venture capital funds that are willing to give small amounts and that are willing to look at the segment of start-ups.*

### What can you do in order to these venture capital funds?

European Commission + European Investment Bank (give loans to bank) has set up a new vehicle = European Investment Funds (EIF)

EIF's objective: invest in venture capital funds. *Only when these funds invest in starters and give small amounts.*

### Why doesn't EIF directly invest in companies? Why do they go through the funds?

- Knowledge: funds know companies better than Europe
- Lot of staff needed if you only invest directly in companies
- EIF can't know all regions
- **Multiplier effect**  
 €1 public money (from EIF) leads to €4 (1+3) investment money (for small companies)  
*Study shows that €1 → VC-policy is 12 - 25 times more efficient than subsidies*  
*EIF funds 800 venture capital funds*

**Can we give money to a company → Competition policy:** policy that should assure that you have equal competition between companies.

*Subsidy in Toyota is unfair competition for Opel.*

General rule: all subsidies are forbidden to companies

Exception: De minimis rule: all subsidies are forbidden unless it goes to SME's and the amount is less than €200 000.

One difficulty with venture capital (not a subsidy) (more like a credit, must be paid back one day)  
 → Subsidy equivalence

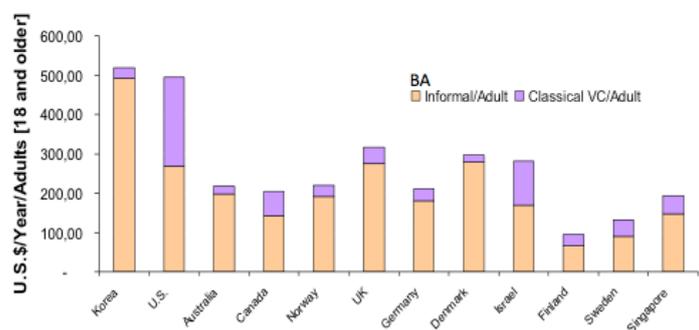
From the competition policy point of view: €500 000 VC equals €100 000 Subsidy (equivalent coefficient)

### 1. The BANs.

The business angels: who are they? 5 Characteristics:

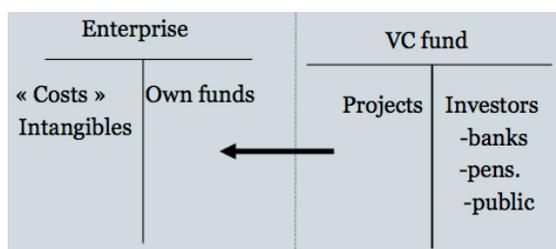
- Enterprise background and managerial experience
- Male, middle aged (Statistics show that)
- Having sold their company (they have time)
- Interested in minority stakes (put money in company but don't want to be the boss)
- 25% of their assets available for informal investments (seeking minimum of 20% return)

Financial Support for Start-Ups: Informal Investments and VC Start-Up Support

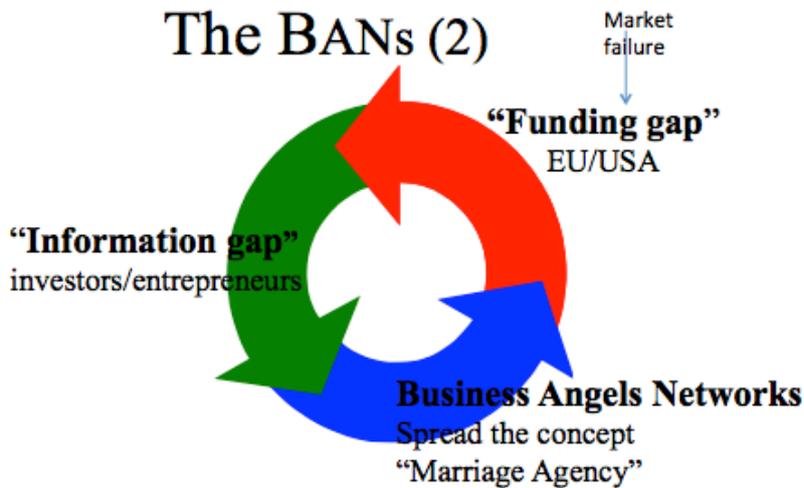


In US: Business angels as important as venture capital  
 In UK: Business angels more important than venture capital

The BANs (1) VC and agency problem



## The BANs (2)



1. Explain how BAN works (spread the concept)
2. Funding gap = market failure
3. Inform both investors (virgin and activa BA) and the entrepreneurs

Those gaps have to be filled from the policy point of view

### The BANs (3) Policy options:

- 1). Fiscal, financial and regulatory environment.

*In France BA don't work very well, Why? Because if in France you take shares of a starting company and the company goes bust, then you're personally responsible.*

*Fiscal: If in Belgium you put €10 000 in a starting company and it works well, and 2 years later you get €50 000 back, there's no **capital gain tax**.*

*In UK, when you're a BA, and you put €100 000 in a company, you'll get directly 20% back from the state in the form of less taxes (Fiscal advantage).*

- 2). Help to the establishment of networks.
- 3). Exchange of best practices (Sweden, UK, The Netherlands).
- 4). Dissemination actions.

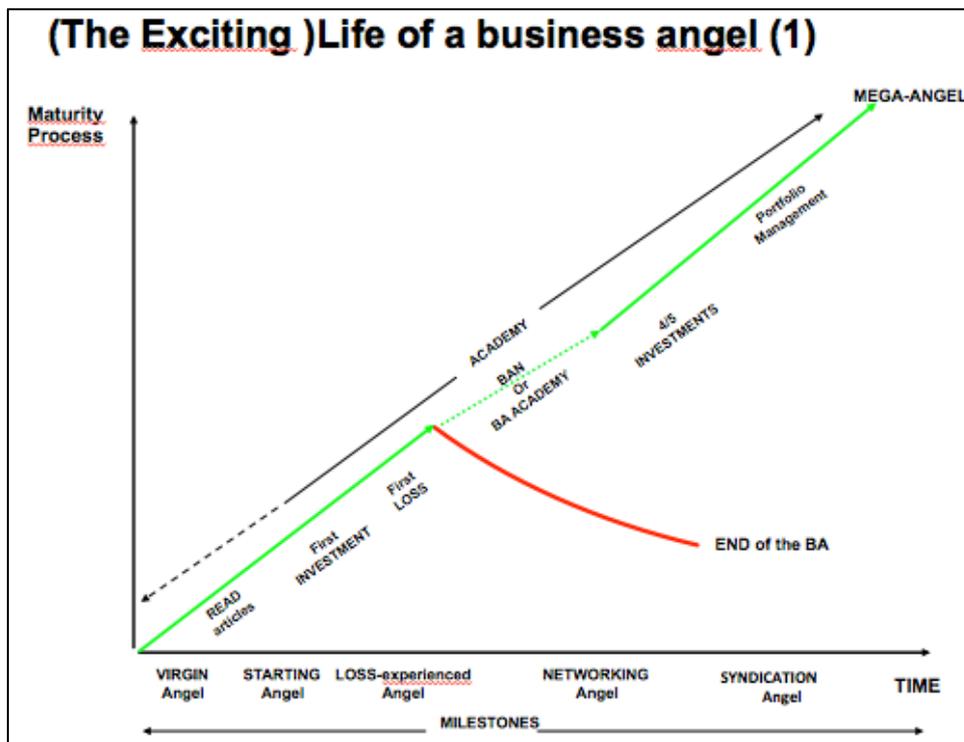
The Commission is financing in whole Europe, seminars where you speak to people with money.

All these lead to the creation of business angels in Europe

### The BANs (4) First attempt of evaluation of policy:

- More networks than deals
  - Deal: BA puts his money in a company
- Most BAN were imbedded in non-profit sector
- BANs are not sustainable
  - Solutions: mergers, consultancy, sponsoring, ....
- The phenomenon remains marginal
- Potential remain highly untapped
- Still a lot of virgins out there
- A hangover syndrome
  - Some BAs regret they're no longer virgins

## 2. (The exciting) Life of a business angel.



You start by being a virgin BA, they read articles and do their first investment.  
In 80% of the cases that leads to a complete loss.

→ Hangover BA, he was a virgin and tried and now will be a virgin for the rest of his live.

Policy issue: how can we make sure that the BA don't stop after the first loss.

It's a learning process, normal that you lose money in the beginning, part of the game.

Instead of putting people together in BAN, should we not consider going back to school? (a lot of people and after their first investments, they stopped, Why is the first investment mostly a loss: wrong sector, they did not analyze the project, not a good value, ...)

Experienced BA should tell Virgin BA how to make the right decisions.

From a Business Angel Network to Business Angel Academy

## 3. The Business Angel Academy

The business angel academy: the aim:

- Creating and educating the market place (*where people shit together*)
- Learning curve for BA (Supply side) (*BA should learn how to invest*)
- Invest readiness for investees (Demand side)
- Creating platforms (demand meeting supply)

BA academy should enable investors to increase their activity for a given deal flow.

The business angel academy: BA: who are they? The five characteristics:

Assumption that if they had the criteria they know how to invest. Wrong, because they have to learn.

The business angel academy: the target group:

- Virgin angels
- “Hangover” angels → invested once, didn’t work, became virgin angel again
- Active angels that could increase their activity → Biggest group at academy
- Potential syndicate angels → angels combining for one project

Who came to the academy? Active angels that could increase their activity.

**4. The IASE experience**

Those who participate in the academy:

- 69% started a business of their own
- 46% still own their business
- On average €500 000 available for investments
- 65% are mentally ready for a total loss
- 85% want involvement in the company (smart money: money + advice + coaching, ...)
- 26 hours a month they want to spend on the company they’ve invested in
- 65% are no longer virgin
- 30% are virgins, they never did it because (Why?):
  - Lack of info on opportunities (75%) (→ initial assumption to create BAN)
  - Not knowing investment procedure (37%)
  - Lack of attractive projects (25%)
  - High risk (25%)

**5. Virgin angels versus active angels.**

Why do active angels want to invest? (Mental attitude: want fun)

- Return
- Challenge
- Advantage of a social network

Why do virgin angels want to invest? (Mental attitude: risk averse)

- Return
- Social benefit
- Support new entrepreneurs

What does the virgin angel vs. active angel expect from the business angel academy?:

BAA's are more efficient than BANs

| Virgin angels                                | Active angels                               |
|--|---|
| Research and evaluation of opportunities     | New business valuation                      |
| Relations with other investors (syndication) | Research and evaluation of opportunities    |
| Growth strategies                            | Growth strategies                           |
| Business plan analysis                       | Business plan analysis                      |
| New business valuation                       | Team management                             |
| Deal negotiation                             | Deal negotiation                            |
| Divestment process                           | Relation with other investors (syndication) |

**6. Conclusions.**

- Informal VC (BA) market considered difficult by active and virgin angels.
- Skills required on Business Plan analysis, growth strategies, divestment and investment process, relations with other investors
- Investment in education is crucial.

→ Plead for BAA and for benchmarking

## 9. Incubators: tool for entrepreneurship.

2 Biggest reasons for bankruptcies:

- Lack of funds → business plan, financial needs are underestimated
- Lack of management skills

35%-40% go bankrupt within the first 3 years.

What happens if you have limited liability (beperkte aansprakelijkheid) and the company goes bankrupt after 5 years?

- I lose injected capital.
  - Can I lose more? NO, unless:
    - 1) Only if company gets credit and they have to give a personal guarantee (collateral: mortgage). It lifts the limited liability.
    - 2) If company goes bankrupt in the first three years, they will look at the business plan.

What can you do in the first case (1)?

→ Always sign as person of company, representative of the company, not sign for yourself

What can you do in the second case (2)?

→ Buy shell company, buy statutes (companies that have seized/stopped their activities) (that are older than 3 years)

If you want to reduce bankruptcy, work at the lack of funds and lack of management skills:

### **INCUBATORS.**

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**Incubator** tries to cope with the two lacks:

- Coaching system (tickets: free advice)
- Smart money (BA/ Seed money) (smart money = money + advice)

*If you say, 'I'll start a company, you can do it on your own, rent a building and do it by myself or you can go to a place with other starters (= incubator). If you go there you get tickets (for fiscal advice, management advice). Europe finances that.*

Incubators have an impact on the default ratio (DR) (probability of a company to go bankrupt).

*Companies that have gotten advice and have smart money have a lower default ratio than companies with dumb money.*

Basel II (BII): **Credit rating = f (DR)**

Because the default ratio is lower, the credit rating also goes down. Cost of credit goes down (= easier access to finance).

### **1) Incubatio: back to basics.**

Incubator (° Incubatio)

Nurturing prematurely born infants, context of controlled conditions: "Couveuse" three objectives:

- To survive
- To grow
- To develop

## 2) Business incubatio:

**Business incubatio:** dynamic process of enterprise development aiming at encouraging people to start their own business and support start-up companies with offices, hands-on management, access to finance, operational know-how,...

**A real incubator is not just office space and shared secretary and fax machine.**

## 3) A real incubator:

**Tenant:** Company in incubator

**Graduate:** Company that leaves/has left the incubator

What are the criteria for an incubator to be efficient?:

- Sufficient number of new, young enterprises **with growth potential** (gazelles)
- Parameters:
  - Optimal **rotation**: (max. 3 years in incubator) **Rotation rate of tenant**.
    - a parameter to know the efficiency of an incubator: rotation coefficient
  - **High survival rate** of graduates
- Incubator has positive impact on entrepreneurship.  
*Imagine that you have next to UGent an incubator, whose focused on young entrepreneurs, on students, who wants to try, but not on their own, with a protective context. They can go to incubator, become a starter, they are protected and after 3 years they leave the incubator.*
- **Links** with industry, R&D, universities
- Structure facilitating **access to finance**: companies in incubator have easier access to finance.

## 4) 5 types of incubators.

Each incubator corresponds to a certain gap.

Mainstream:

- **Mixed incubators**: mix of companies, *Only reason for mix incubator?* to have more businesses. Mixed incubator tries to cope with the **business gap**.
- **Economic development incubator**: not linked to business, but linked to regions that are lagging behind. This incubator tries to cope with **regional and local disparity gap**.
- **Technology incubators**: focus on the **entrepreneurial gap**. Incubator is focused on kind of technology. Media-incubator.

Specific:

- **Social incubators**: incubator on a certain target group. Tries to cope with the **social gap**.  
*Incubator on long-term unemployed people, to go there as a company, the starter has to be someone who has been unemployed for over 3 years. (Gent)*  
*Incubator with only women.*
- **Basic research incubator**: puts together different scientists from different fields. Tries to cope with the **discovery gap**.  
*Examples: MIT, IET, Starlab*

**5) History: from bricks to BIC (Business Incubator Center) to clicks.**

US:

**Mixed incubators:**

- in '50/'60: revitalizing declining areas/plant closures.  
*First incubator: Detroit: after car industry left, there were big plants, qualified people and buildings. First incubator always linked to declining area.*
- in '70/'80: fostering emerge of innovative companies
- '90: targeted technology incubator; new economy

Europe:

**Mixed incubators**

- since mid '70: revitalizing declining areas/plant closures/UK
- '80: Innovative companies  
European Commission decided to finance these incubators everywhere in Europe.  
**BIC:** business incubator center → mostly economic development incubators. (Germany/FR)
- '90: targeted technology incubators; new economy

**6) Incubators of the 21<sup>st</sup> century.** Clicks no bricks

Develop incubator around specific industrial and technological cluster involving different partners.

**Virtual incubators.**

*Speed technology, bio-technology (VIB (Gent)), IMEC (nanotechnology), Sofia antipolis.*

**7) US performances by different types.**

|                         | Mixed | Ec. dev. | Techno | Average |
|-------------------------|-------|----------|--------|---------|
| Square feet             | 36314 | 30833    | 31041  | 32729   |
| Survival rate           | 87%   | 86%      | 90%    | 87%     |
| Tenants/<br>incubator   | 15,3  | 20,3     | 13,7   | 16      |
| gazelles ← Empl/tenants | 64    | 84       | 248    | 132     |
| Empl/<br>graduates      | 196   | 95       | 430    | 240     |
| Graduates/<br>community | 97%   | 95%      | 97%    | 96%     |

Survival rate is very high.  
Starting a company in incubator decreases risk of bankruptcy within 3 years.  
**Incubator are good tool for reducing the risk of bankruptcy.**

Which incubators are the less efficient in terms of policy? Economic development incubators.  
Why? Because these are mostly concentrated in difficult regions.

Another parameter:  
•measure by job creation  
•Local link – local employment – local investment

Graduates stay within their community. Incubator very good tool for regional employment.

**8) Europe's mosaic.**

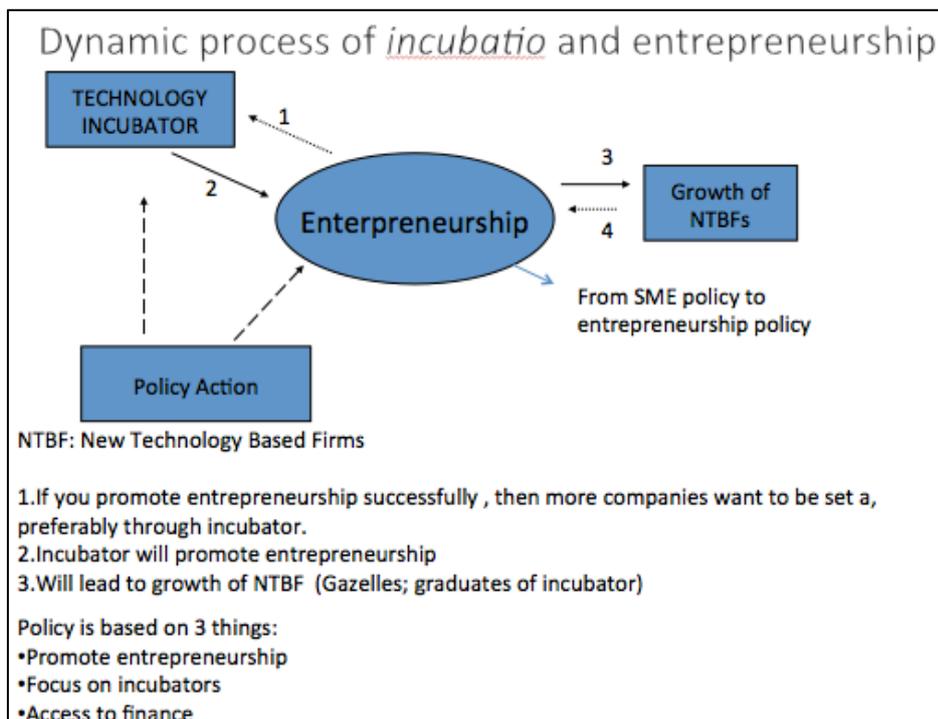
Europe is very fragmented:

- The BIC network
  - 150 BICs in Europe

Different approaches:

- **The Anglo-Saxon approach:** linked to university, mostly focused on spin off: start-up based on research at the university. *Example: Cambridge-incubator.*  
**Main income of incubator:** Royalties (intellectual property rights); success fee.
- **The Germanic model:** in the middle
- **The Latin approach:** incubator becomes real estate, nice building, starter doesn't leave (*if other starter goes bankrupt, you can get his office too*). More like renting offices.  
**Main income of incubator: Rent.**
  - Very low rotation ratio.

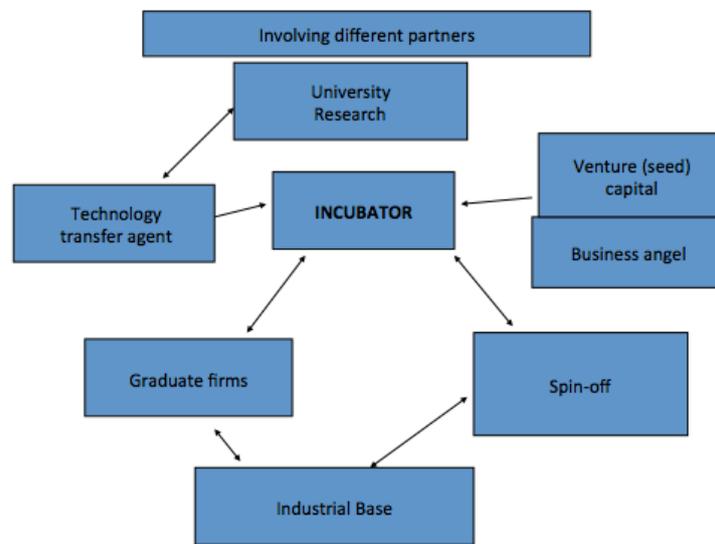
### 9) Dynamic process of incubation and entrepreneurship.



### 10) Promote development of New Technology Based Firms (Gazelles, NTBF).

Incubatio:

- Promoting entrepreneurship
- Technology commercialization
- Offering credibility
- Venture capital and assessment
- High value-added services
- Real estate
- Legal advice, marketing advice.



Core = Incubator

Incubator needs, in order to be efficient, an in-house (involved in incubator)

- venture (seed) capital
- business angel
- Technology transfer agent: Agency who takes ideas from universities, protect them (patent) and value them.

Incubator can lead to graduate firms, can lead to spin-off, that creates an industrial base.

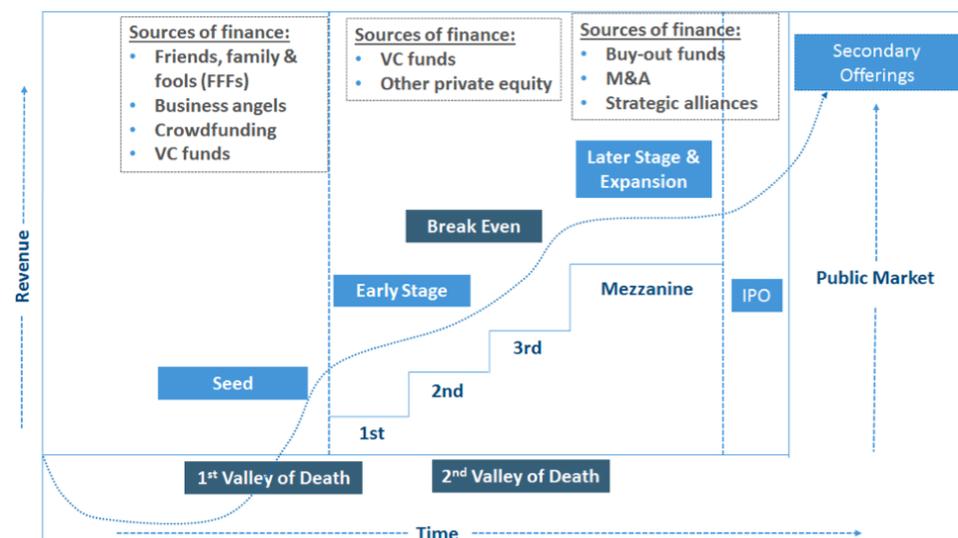
Companies concentrate around the incubator.

### 11) Benchmarking framework

- Success factors in establishing and operating incubators
- Nature and scope of support services
- Key functions of incubator managers
- Promotion of incubator services
- Evaluation of incubator services

## 10. Two valleys of death

→ Market failures in equity



How much goes into that gap?

Not an exact science:

- Deloitte: EU: demand: 50 to 80 bn – supply: 11, gap: 40 to 70 bn €
- Breughel think-tank: twice as big in EU than US
- de Silanes et al: EU: 500 bn \$; US: 200 bn \$
- Mc Kinsey: equity gap will continue to grow: by 2020: 12 trillion \$ (estimation 2011)