

# Nordic-European Public Investor Initiative

Experience sharing & Joint advice on EU policy  
*November 2012*





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Industrifonden, Sweden

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Estonian Development Fund, Estonia

Scottish Enterprise, Scotland

Bayern Kapital, Germany

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## **Coordinator of the Initiative**

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# 1 Executive summary

## **Public efforts needed**

The European venture capital market is under severe pressure. Several factors have combined to make it difficult for private venture capital funds to raise capital for new funds, including lack of financial returns, the financial crisis and new regulations for banks and other investor categories.

European countries have implemented and are planning further large-scale initiatives to ease the situation, which would otherwise have major implications for promising European high growth companies that are expected to create future industries and employment.

The Nordic Council of Ministers recognises the importance of seed and venture capital and since 2004 has commissioned several projects aimed at promoting a well-functioning common Nordic venture capital market. As the previous Nordic initiative model proved successful, the idea emerged of broadening the scope by combining Nordic public investors and other leading European investors in a Nordic-European initiative, about which talks have been held with European Commission representatives.

In 2010 a decision was taken to launch a two-year Nordic-European Public Investor Initiative in 2011-2012. The Initiative fulfils a dual purpose. First, it strengthens the effect of public investment in venture capital by a greater level of interaction and cooperation as well as experience sharing between Nordic and other European public direct investors. Second, it influences the EU decision-making process to make well-informed design of new programmes and initiatives.

The Initiative is organised by Nordic Innovation, an organisation under the auspices of the Nordic Council of Ministers, and comprises a network of 11 national public investors in the field of seed capital and venture capital with 3.2B EURO under management and more than 1,600 portfolio companies as well as the European Investment Fund. The Initiative members are drawn from 8 northern European countries.



**The joint report – policy advice and experience sharing**

The present report, “Nordic-European Public Investor Initiative - Experience sharing & Joint advice on EU policy” has a dual content. It first describes the joint policy advice presented by the Initiative to the EU Commission regarding structural fund regulations in the 2014-2020 programming period. Secondly, the report includes brief descriptions of existing programmes and models used in the different European countries in which the member organisations are based.

The members of the Nordic-European Public Investor Initiative jointly produced the report, while the national sections were individually written by the members from the respective countries.

In October 2011, the European Commission proposed a cohesion policy legislative package for the period 2014-2020. The package was designed to boost growth and jobs across Europe by targeting investment as part of Europe's Growth and Jobs Agenda (“Europe 2020”). The package included an overarching regulation setting out common rules for the European Regional Development Fund (ERDF), the European Social Fund (ESF) and other so-called EU structural funds. It also contained three specific regulations for the ERDF, the ESF and the Cohesion Fund.

The so-called structural funds are important sources of capital for the national European venture capital markets. The members of the Initiative have vast experience of EU financial instruments and deep insights into the function of the various national venture capital markets.

Therefore the Initiative took an early decision to submit a joint response to the suggested structural fund regulations for the 2014-2020 programming period. This response was discussed at a workshop and summit in Stockholm during autumn 2011.

Mr Jean-David Malo, Head of Unit, EC - DG Research and Innovation - Directorate C Unit C03, and Mr António Gonçalves, Head of Unit, D3 Financial Engineering, major projects - DG Regio, participated in the Nordic-European Public Investor Summit in Stockholm on November 24th, 2011, along with many other speakers.

The joint response was submitted to the EU Commission on January 6<sup>th</sup>, 2012, and the main points in the document can be summarized as follows:

- Market practice should be the overall principle for financial instruments
- Private sector leverage is key
- Financial engineering instruments rather than grants play a key role in creating competitive European growth companies
- Financial instruments should be available early in the programming period

- The discrepancy between Fund and programming period life cycles should be minimised
- Fee structures should be set according to market practice
- Pan European funds should be enabled
- More flexibility should be allowed in new instruments
- Realistic time scales for financial instruments are important

The national sections in the second part of this report include introductions to the national markets, an overview of national public direct investors as well as an update on experiences and current developments.

Different models have been used in the various countries, ranging from publicly funded private regional funds, via co-investment schemes with angel investors to direct public investments with active ownership. The suitability of the models depends on the stage, industry focus, characteristics and development of the different national markets.

The national overviews are intended as an introduction to and mapping of the national public direct investors. Much more can be learned about them by visiting their websites, links to which are included in the national sections.

Currently Governments are changing the organization of direct public investment in many European countries in order to promote more effective public efforts. Information about this can be found in the national sections.

The focus of this report is on direct public investors. In addition to direct investments, Governments also invest in private venture capital funds through so-called fund-of-funds.

#### **Active measures needed for public investor interaction**

National public investors are mostly restricted to investing in their country of origin, which means that they seldom do business with each other. Despite the fact that to a great extent the investors face similar challenges, active measures such as this Initiative are necessary in order for them to interact, share experiences as well as investment models. By joining forces and sharing experiences, Nordic and other European investors can become more effective in supporting the growth and internationalization of innovative companies.

This report also serves as a closing document for the two-year Initiative and will be published at the Nordic-European Public Investor Workshop on November 28<sup>th</sup> in Stockholm.

## 2 Introduction and context

### 2.1 Background

The European venture capital market is under severe pressure. Several factors have combined to make it difficult for private venture capital funds to raise capital for new funds, including:

- Lack of attractive returns from European venture capital funds after the Internet bubble
- The financial crisis has made investors more risk adverse with a greater tendency to shy away from high risk investments
- New regulations governing banks and other investor categories have made Investments into venture capital funds more difficult

For example, in a study conducted by Preqin<sup>1</sup>, 26% of European banks had either ceased investing in private equity or reduced their level of activity in this asset class due to regulatory changes.

European countries have implemented and are planning further large-scale initiatives to ease the situation, which would otherwise have major implications for promising European high growth companies that are expected to create future industries and employment.

The Nordic Council of Ministers has recognised the importance of seed and venture capital and commissioned several projects aimed at promoting a well-functioning common Nordic venture capital market.

Since 2004, a number of venture capital projects have been carried out by Nordic Innovation, an institution under the auspices of the Nordic Council of Ministers. In a number of cases, the findings and recommendations have contributed to policy change in the Nordic countries. For example, some restrictive mandates for public investors in funds have been changed from being strictly national to allowing Nordic investments. In addition, obstacles to cross border investments in Nordic private equity structures have been and are being eliminated.

1) Preqin Special Report: Banks as Investors in Private Equity, 2012, Preqin Ltd.

As the previous Nordic initiative model proved successful, the idea emerged of combining Nordic public investors and other leading European investors in a Nordic-European initiative, thus broadening the scope. Talks were held with representatives of the European Commission.

The European Commission is an important organisation for the European market due to, among other initiatives, the so-called Structural Funds. One of the goals of the overall EU 2020 strategy is to improve framework conditions and access to finance for research and innovation in order to strengthen the innovation chain and boost investment levels throughout the EU.

In 2010 a decision was taken to carry out a two-year Nordic-European Public Investor Initiative during 2011-2012.

## 2.2 The Nordic-European Public Investor Initiative

### 2.2.1 Purpose and targets of the Initiative

The Nordic-European Public Investor Initiative fulfils a dual purpose. First, it strengthens the effect of public investment in venture capital by a greater level of interaction and cooperation as well as experience sharing between Nordic and other European public direct investors. Second, it influences the EU decision-making process related to new programmes and initiatives.

The timing of the Initiative, 2011-2012, coincides with the introduction of new EU Structural Fund regulations for the programming period 2014-2020.

The fact that the private venture capital market in Europe is under pressure has increased the importance of public investors. By joining together under the umbrella of Nordic Innovation, Nordic and other European public direct investors will be able to enhance the output of the various national and European initiatives and investment schemes through active experience sharing, focused discussions and concrete policy advice.

On a European level the EU has created a 10-year strategy "Europe 2020" aimed at smart, sustainable and inclusive growth. One of the goals is to improve framework conditions and access to finance for research and innovation in order to strengthen the innovation chain and boost levels of investment throughout the EU. There are today a number of important programmes and initiatives at European level and the design of new programmes is being discussed and negotiated.

The primary goals of the Nordic-European Public Investor Initiative are to:

- influence the EU decision making process in relation to new programmes and initiatives for financing European companies
- establish a deeper dialogue and experience sharing among European public direct investors
- develop and intensify cooperation between European public investors
- discuss how more early stage private investments can be generated
- provide input and advice to Nordic Innovation and others regarding venture capital financing projects and the development of start-up companies

Increased interaction and experience sharing will lead to greater effectiveness in and enhanced output from European public venture capital investment in high growth companies. Concrete advice to political decision makers will enable the well-informed design of new public initiatives, while taking account of existing initiatives.

### **2.2.2 Organisation of the Initiative**

The Nordic-European Public Investor Initiative marks the first time that leading Nordic and other European public direct investors in venture capital have cooperated in one project.

The Initiative is organised under the auspices of Nordic Innovation and comprises a network of 11 national public investors in the field of seed capital and venture capital funds with 3.2B EURO under management and more than 1,600 portfolio companies as well as the European Investment Fund. The Initiative members are drawn from 8 northern European countries.

Today, public investors in venture capital invest in a number of different forms and in all phases of a company's development, from the early stages to expansion.

For the sake of simplicity, public investors can be divided into two categories: Indirect asset management investors, i.e. investors in various categories of private equity funds, so called fund-of-funds investors, and Direct investors, which is the group focused upon by the Nordic-European Public Investor Initiative.

In this report and context, Direct investors are those who invest directly in companies, coordinate regional or specialized publicly financed funds, in addition to those financed by the European Commission Structural Funds or who work with co-investment schemes including private investors such as family offices and the so-called business angels.

The Initiative focuses on Direct investors as a complement to broader networks or initiatives, as they face similar tasks and challenges and use the same type of models and tools when investing in young promising companies.

Despite more or less similar challenges, experience sharing and cooperation between active Direct investors in venture capital in different European countries has so far been limited, the main reason being that the investors operate in different geographical areas.

**Owner of the initiative:**

Hans Christian Bjørne, Nordic Innovation

**Initiative coordinators:**

Erik Johansson & Carl-Peter Mattsson, Nordic Investment Solutions<sup>2</sup>

**Members of the Initiative**

Finnvera, Finland  
Finnish Industry Investment, Finland  
Innovation Norway, Norway  
Investinor, Norway  
Innovationsbron, Sweden  
Industrifonden, Sweden  
NSA Ventures, Iceland  
Estonian Development Fund, Estonia  
Scottish Enterprise, Scotland  
Bayern Kapital, Germany  
Krajowy Fundusz Kapitalowy, Poland

**Associate member of the Initiative**

European Investment Fund, EIF

**2.2.3 Activities to date**

In 2011 a Nordic-European Public Investor Summit took place in Stockholm. It was a focused gathering of European Direct investors in early stage and venture capital, political decision makers, selected public fund-of-funds investors as well as other relevant actors.

Given the purpose of the Initiative to provide concrete advice in direct dialogue with the European Commission, Mr Jean-David Malo, Head of Unit, EC - DG Research and Innovation - Directorate C Unit C03, and Mr António Gonçalves, Head of Unit, D3 Financial Engineering, major projects - DG Regio, participated along with many other speakers.

2) Nordic Investment Solutions is a Nordic advisory firm within private equity.([www.nordicinvestment.se](http://www.nordicinvestment.se))

Prior to the Summit, a Workshop was held between the members, the main purpose of which was to discuss and agree on clear joint advice pertaining to EU policy for the 2014-2020 programming period. A joint response to the proposed regulations for so-called “Structural funds” was submitted to the EU Commission on January 6, 2012.

The dialogue with the EU Commission on EU regulations has continued during 2012. Representatives from the Initiative will participate at consultancy sessions with the Commission on regulations for financial instruments. Individual members have worked with different parts of the Commission as well as national governmental agencies regarding the negotiations for the 2014-2020 period.

During autumn 2012 the members will gather for a Workshop to continue discussions on joint policy advice, share experiences of models and determine the main challenges facing European public investors going forward.

## 2.3 The joint report

This report has a dual content. It first describes the joint policy advice presented by the Initiative to the EU Commission regarding the regulations for Structural Funds in the 2014-2020 programming period. Secondly, the report includes brief descriptions of existing programmes and models used in the different European countries in which the member organisations are based.

The members of the Nordic-European Public Investor Initiative have jointly written the report, and the members from the respective countries have individually written the national sections. The editor of the report is Erik Johansson, Managing Partner at the coordinator for the Initiative, Nordic Investment Solutions.

The scope of the report does not include deep analysis of the forthcoming EU Structural Fund regulations or the national investment models. Its purpose is to provide an introduction and overview of the themes to inspire further interest and discussion.

The report also functions as a closing document for the two-year Initiative and will be published at the Nordic-European Public Investor Workshop on November 28th. in Stockholm.

## 3 Joint advice on EU policy

### 3.1 Introduction to joint advice on EU policy

One of the goals of the overall EU 2020 strategy is to improve framework conditions and access to finance for research and innovation in order to strengthen the innovation chain and boost investment levels throughout the EU.

In October 2011, the European Commission proposed a legislative package for cohesion policy for the 2014-2020 period. The package was designed to boost growth and jobs across Europe by targeting investment as a part of Europe's Growth and Jobs Agenda ("Europe 2020").

The package included:

- An overarching regulation setting out common rules governing the European Regional Development Fund (ERDF), the European Social Fund (ESF), the Cohesion Fund, the European Agricultural Fund for Rural Development (EAFRD) and the European Maritime and Fisheries Fund (EMFF).
- Three specific regulations for the ERDF, the ESF and the Cohesion Fund

The proposals are currently being discussed by the Council and the European Parliament to be adopted at the start of a new generation of cohesion policy programmes in 2014.<sup>3</sup>

As stated above, one of the main targets of the Nordic-European Public Investor Initiative is to influence the EU decision-making process in relation to new programmes and initiatives for financing European companies.

The so-called structural funds are important sources of capital for national European venture capital markets. The members of the Initiative have vast experience of EU financial instruments and deep insight into the various national venture capital markets. Therefore the Initiative took an early decision to submit a joint response to the suggested regulations for the structural funds for the 2014-2020 programming period, which can be found in the next section.

<sup>3</sup> European Commission Press Release, Brussels, October 6th, 2011



## 3.2 Joint response to the draft Structural Fund regulations for 2014-2020

Below follows the Nordic-European Public Investor Initiative's joint response to the European Commission's consultation on the draft Structural Funds Regulations for the 2014-2020 Programming Period as submitted on January 6, 2012:

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*Nordic-European Public Investor Initiative response to the European Commission's consultation on the draft Structural Funds Regulations for the 2014-2020 Programming Period*

As representatives of public investors in the field of financial instruments, we very much welcome the opportunity to comment on the Commission's draft Regulations for the 2014-20 Programming Period.

The Nordic-European Public Investor Initiative is a network of 11 national public investors in the field of seed capital and venture capital funds as well as the European Investment Fund. The initiative members are drawn from 8 countries in northern Europe and together the 11 national investors have over 1600 portfolio companies and more than 3.2B EURO under management. The Initiative is owned by Nordic Innovation an institution under the Nordic Council of Ministers facilitating sustainable growth in the Nordic region. Coordinator for the Initiative is the Nordic independent private equity advisory firm, Nordic Investment Solutions.

The Initiative is aimed at formulating practical measures to develop effective financial instruments as well as facilitating exchange of best practice in the field of risk capital among

its members. The purpose of this paper is to respond to the Commission's Consultation through a joint contribution by the Initiative.

The members have considerable combined experience in investments from seed to IPO as well as fund-of-funds. The members have extensive knowledge and long experience of developing and implementing public policy to address market failures in the European early stage risk capital markets, as well as utilizing large scale ERDF in the capitalization of financial instruments to address such gaps. Some of the members of the Initiative have been utilizing ERDF in the creation of financial instruments since the 1994-1999 Programming period, and have refined and developed their approach to addressing market failure over successive Programming periods. Further, the members are highly active investors, facilitators and opinion leaders in their respective countries and demonstrate innovation, growth creation, exemplary governance and world-class success stories.

The members strongly support the Commission's intent to increase the use of ERDF in order to extend the scale and scope of financial instruments, which improve access to finance for SMEs. We welcome the opportunity extended by the Consultation to make suggestions which we hope will improve and enhance the positive draft proposals regarding financial instruments.

The members of the initiative have agreed on a number of suggestions on the proposed ERDF Regulation (*SEC(2011) 1139 final*) with the intention of increasing the usefulness and impact of the regional Structural Funds. **We would welcome the opportunity to continue this dialogue with the European Commission as the Regulations are developed further.**

The purpose of these suggestions is to strengthen the competitiveness of European business life by growing companies of scale on a local, regional, national as well as European level.

The members of the initiative acknowledge the proposed scope of the ERDF, in particular *productive investment and research & innovation* in Article 3 of the proposed Regulation laying down specific provisions of the ERDF. We also acknowledge the proposed investment priorities in Article 5, most notably: (1) *strengthening research, technological development and innovation* and (3) *enhancing the competitiveness of SMEs*, respectively.

The members of the initiative strongly support the importance of the following sections set out in the in the preamble of the proposed legislative package, for the purpose of developing high growth, world class, European companies in cooperation with private investment. The following suggestions are intended to further enhance these sections:

- Whereas (24): Financial instruments should be designed to promote private sector investor participation on an appropriate risk-sharing basis.

- Whereas (25): Giving managing authorities full flexibility to use financial instruments set up both at EU and regional level, and permitting both direct investments and fund-in-fund solutions.
- Member States should be allowed to continue using instruments adapted to their specific regional conditions. Implementing rules should be simplified and stated clearly to enable this.
- The members support the principle of maximizing private investor participation in equity financing instruments and believe that market oriented principles should always be applied.
- The assumption in applying ERDF to financial instruments should always be that the public sector operates on an as commercial basis as possible, applying the Market Economy Investor (and where appropriate Lender/Guarantor) Principle. Therefore ERDF interventions in financial Instruments should only be subject to a State aid assessment when the applicant deviates from commercial practice.

The members of the initiative suggest the following amendments and seek clarification regarding the proposed ERDF Regulation:

- **Market practice the overall principle.** The overall principle should be that implementation rules are to be brought into line with market practice;
- **Private sector leverage.** Financial instruments should address market failure in a manner that stimulates, rather than competes with, existing private sector provision so that high levels of additionality are secured.
- **Financial engineering instruments as opposes to grants play a key role in creating competitive European growth companies.** ERDF resourcing of financial instruments has grown in importance over successive Programming periods, from 1% in 2000/6, to 5% in 2007/13. We propose that a minimum

of 15% of ERDF resources should be allocated to financial instruments, and that Member States should be allowed to further increase this threshold in their regions. Equity investments in enterprises generate more added value, leverage private investment, and provide long term sustainability. ERDF resources to traditional grants should decrease considerably in volume, since they cannot be re-used and tend to fund short-term projects (e.g. three years) that are often discontinued as soon as funding stops;

- **Financial instruments early in the period.**

Financial instruments should ideally be set up at the beginning of the 2014/20 Programme in order to maximise their contribution to the Europe 2020 targets, and therefore financial resources should be available early in the time period to allow for this;

- **The discrepancy between Fund life cycles and Programming period life cycles should be minimized.**

The life cycle of early stage funds is significantly longer than that of a Programming Period, with disbursements taking place throughout the whole life cycle of the fund, including follow on investments into portfolio companies. This gives rise to difficulties in accounting and claiming for expenditure beyond the Programming Period, which mitigates against public investors' ability to operate on a fully commercial basis. For example, a typical VC fund manager will set aside c.25% of Fund capital value for follow on investments (acting commercially). Whilst the initial investment will have been made during the Programming Period, follow on investment necessary to reach commercialisation will fall out with the Programming Period. The Commission may wish to consider how such anomalies can be reconciled;

- **Fee structures according to market practice.**

Management fees for venture capital funds should reflect market practice to enable the engagement of professional staff. Highly professional and experienced staff is a prereq-

uisite for executing successful investments into SMEs. Market practice can be found by investigating and describing fees for private funds.

- **Pan European funds should be enabled.**

Managing Authorities should have possibility to broaden focus beyond the Member State level and thus be able to participate in pan European funds;

- **More flexibility in new instruments.**

We welcome the Commission's proposal to design ready-made financial instruments at EU level, which can be readily adopted by Member States. New instruments should provide more flexibility and include a facilitation of investments in early stages of company development. Regulations for new instruments should be as clear and as easy to implement as possible to enable effective usage. In the interests of subsidiarity and partnership, we suggest that it should be for the Member State to decide the most appropriate financial instrument, be that 'ready made', EU wide, national or regional, existing or new. These will, of course, fit with the ex-ante assessment prepared by the Member State at the start of the Programming Period.

- **Realistic time scales for financial instruments.**

It is worth noting that a realistic financial returns timescales for financial Instruments at early stage extends well beyond the 2014/20 Multi Annual Framework. We suggest that this should be taken into account when setting targets relating to financial instruments in Partnership Agreements;

- **Working capital.**

Financial instruments addressing early stage market failure can claim working capital as eligible expenditure. The Commission may wish to consider extending this to new financial instruments for established SMEs for the duration of the current financial crisis where many established SMEs are experiencing difficulties in securing bank finance;

- **Ex anti assessments.** We commend the Commission's proposal that Member States/ Managing Authorities should conduct ex-anti assessments prior to supporting financial instruments. This is established practice for some of the members of the Initiative and we would welcome the opportunity to discuss how this proposal could be practically implemented.

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Date: 6 January 2012  
Submitted by: Nordic-European Public Investor Initiative

**Members of the Nordic-European Public Investor Initiative**

Veraventure, Finland  
Finnish Industry Investment, Finland  
Innovation Norway, Norway  
Investinor, Norway  
Innovationsbron, Sweden  
Industrifonden, Sweden  
New Business Venture Fund, Iceland  
Estonian Development Fund, Estonia  
Scottish Enterprise, Scotland  
Bayern Kapital, Germany  
Krajowy Fundusz Kapitalowy, Poland

**Associate Member of the Nordic-European Public Investor Initiative**

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## 4 Introduction to national sections

The national sections below include introductions to the national markets, an overview of national public direct investors as well as an update on experiences and current developments. The members from the respective countries have individually written the national sections.

Different models have been used in the various countries, ranging from publicly funded private regional funds, via co-investment schemes with angel investors to direct public investments with active ownership. The suitability of the models depends on the stage, and industry focus, characteristics as well as the development of the different national markets.

The national overviews are intended as an introduction to and mapping of the national direct public investors. Much more can be learned about them by visiting their websites, links to which are included in the national sections.

Currently Governments are changing the organization of direct public investment in many European countries in order to promote more effective public efforts. Information about this can be found in each of the national sections below.

# 5 Finland – overview of direct public investors

## 5.1. Introduction to the Finnish market

The Finnish Venture Capital market has witnessed the withdrawal of several players in recent years. Although this caused some imbalance in the market, it has been compensated by the increased activity of international VC funds in Finland. Almost all pre seed and seed stage VC is provided by public investors. Some pension funds have entered the market at a later stage through a small number of direct investments, whereas investments into VC funds have been rare.

A major change in the early stage community has been a movement known as “Helsinki Spring” i.e., a student movement that has made becoming an entrepreneur a serious career option. Aalto Entrepreneurship Society ([www.aaltoes.com](http://www.aaltoes.com)) has been the driving force in the movement. However, more private capital is needed to boost this phenomenon.

The angel market in Finland is making slow but steady progress. Angel investments are estimated to be some 30-40 MEUR annually. The largest angel network is “InvestorExtra” run by Finnvera venture with some 250 members. The second largest network is FIBAN, the Finnish Business Angel Network, with approx. 150 members. From the beginning of 2013 these two networks will be merged creating there by a network of over 300 members. Angel investments are believed to increase in 2013 as the Finnish government has decided to introduce a tax break for new angel investments.

## 5.2 Direct public investors

Finnish Industry Investment Oy (FII) ([www.industryinvestment.com](http://www.industryinvestment.com)) promotes Finnish business, employment and economic growth through venture capital and private equity investments. FII invests in funds and directly in growth companies in all sectors with focus on growth, internationalisation, spin-offs, major industrial investment as well as sectorial and corporate restructuring. The investment model is based on market terms and applies the syndication principle. FII has capital under management worth 700M EUR.

In Finland, the public VC funding in the seed phase is organised through Finnvera plc ([www.finnvera.fi](http://www.finnvera.fi)), a State owned special funding agency that also provides export credits, project finance in addition to loans and guarantees for SMEs. Finnvera started early stage investing in 2006 by creating, as an experiment, a small 13.5M EUR evergreen fund for seed investments. Encouraged by the quality of the deal flow, the capital base of the fund has been raised to 113.5M EUR and there are plans to increase the fund size to 150 M EUR by 2013. Some 170 investments have been made and the current activity is approx. 20 new investments annually. A typical initial investment is 300K EUR. With add-on investments the fund can invest up to 2.5M EUR in a target company.

Sitra ([www.sitra.fi](http://www.sitra.fi)) is an organisation under the supervision of the Finnish Parliament. Sitra's investment portfolio comprises around 50 enterprises with a total investment of approximately 124M EUR. Most enterprises are in the medical industry, followed by biotechnology, industrial products and services. Sitra invests through focused programmes. Current programmes include the energy sector and clean technology. Sitra also operates as a fund investor.

## 5.3 Experiences and current developments

### 5.3.1 Experiences from public investment models

Seed stage VC is an ideal arena for public investors. Public intervention is well justified due to the lack of private investors. Finnish experiences from Finnish Industry Investment and Finnvera have shown that the syndication model works extremely well in early stage investments. Public and private investors investing together on symmetrical terms produce the best results with regard to the business development of the young firm and contribute best to future investment rounds.

Partnering with private investors also causes less market disturbance. Later stage investments should be more private investor driven and there, with public investors acting as co-investors, sharing risk, contributing to diversification of portfolios and adding financial resources to financing rounds.

### 5.3.2 Current developments and recommendations

Tax incentives has probably not been exploited to their full potential in Finland. For example, business angel activity, especially in early stage investments, could be significantly boosted by tax exemptions on venture capital investments and their capital gains. There is a great deal of evidence of this from several countries, e.g., the UK. Such a tax incentive could also encourage family offices and foundations to invest in VC funds. To use this potential the Government has decided to implement tax incentives for business angels starting in 2014.

Government has also decided that Tekes ([www.tekes.fi](http://www.tekes.fi)), the Finnish Funding Agency for Technology and Innovation, will start doing direct seed investments during 2013. Tekes today primarily finances business research and development programs.

On the EU level, it might be worthwhile to explore the possibilities of channeling EU funding into regional venture capital markets through national public investors. This funding should not originate from the Structural Funds and as far as possible be on commercial terms but with more lenient conditions.

It is also quite common that funds financed through the Structural Funds or that have notified their operations with the Commission are geographically limited in terms of their investment activities. In order to create companies with critical mass that can enter the international market, more cross border investment within the EU should be encouraged when there is sufficient local interest to make investments outside the home base of a fund.



# 6 Norway – overview of direct public investors

## 6.1 Introduction to the Norwegian market

The following is an update of the status of the Norwegian venture capital and early stage markets together with the main challenges and issues that need to be resolved from the perspective of Innovation Norway and Investinor. An overall description of direct public investors and their investment models and schemes is provided. Examples of different public investment models and recommendations for potential new models are also discussed.

The VC and seed capital sector is important for the creation of new companies and industries in Norway. Together with research facilities, incubators, science parks and later stage investors, it forms an eco-system that helps to increase the number of young growing companies.

The supply of seed capital in the Norwegian market has been low. Today, almost 90 % of the capital in this segment is provided by public schemes. Apart from within public operations, seed capital is very limited, despite the emerging trend of early stage private investment.

The overall Norwegian private equity market has experienced strong growth over the past decade. In Norway, private equity financing has traditionally been provided by family-owned companies, generally as a secondary activity to their primary business. It is only in the past 10-15 years that a professional fund management industry based on institutional capital has emerged. The local private equity market is organised around industrial clusters such as oil and gas, marine and maritime, technology, media and telecom industries. Some oil and gas focused private equity funds have backed innovative high growth companies and produced world class returns.

In terms of activity, the Norwegian private equity sector was previously more oriented towards venture capital than was usually the case internationally. However, during recent years, several new mid-buyout funds have been established, which have raised substantial amounts of capital.

Some of the major challenges facing today's Norwegian seed and VC markets are:

- Relatively low supply of seed capital.
- Private capital in the seed stage is still too limited.
- Fundraising for venture capital funds has become more difficult and the venture capital firms still need to prove their long-term competitiveness. These firms are important follow-on investors with which the seed investors can cooperate.
- Long-term financing should be provided for venture capital funds to ensure the evolution of experienced Norwegian venture capital firms.

## 6.2. Direct public investors

Below is an overview of the main direct public investors in Norway.

### **Innovation Norway**

Most public financing facilities for SMEs in Norway are combined in one organisation, Innovation Norway ([www.innovationnorway.no](http://www.innovationnorway.no)). The mission of Innovation Norway is to contribute to the development of Norwegian business life, both nationally and internationally, with focus on nine strategic areas, including energy and the environment, ICT, oil and gas, maritime and marine. The organisation provides services and programmes aimed at developing the regions, increasing the level of innovation in businesses all over the country and promoting Norwegian business and tourism.

In 2009 Innovation Norway contributed about 8B NOK of grants and loans to development projects. 85% of this financing was directed towards companies with less than 20 employees.

Innovation Norway has organised seed capital funds since 1998. Today there are 15 separate funds, of which 5 are national while the others are regional. All of the funds are made up of substantial public financing, part of which is allocated as a loss fund that can be used when holdings are fully written off.

The funds and fund managers are privately owned although 50 - 70 % is financed by public means. The funds in turn invest in portfolio companies. The seed capital funds were established in two waves, 1998-2000 and 2006-2008. These funds have a total capital of 3.1B NOK. The funds organised by Innovation Norway only invest in Norway.

An analysis of the first wave of publicly financed funds revealed that to date, these funds have had much lower returns than anticipated. Evaluations demonstrated that with the exception of one fund, all have had negative returns. A mere three out of 175 investments were sold at a high profit.

More recent funds have a higher capital base, larger specialised management teams and invest greater amounts in each company. It is still too soon to judge the performance of these funds, but they have already had four exits with 2x multiples or more. The number of failed investments is lower than in the first wave when comparing the funds at the same point in their investment period. The 2009 evaluation revealed that the more recent funds added more competencies to their portfolio companies than the first wave.

### **Investinor**

In 2008 a new Government funded investment company, Investinor AS ([www.investinor.no](http://www.investinor.no)), was established in Trondheim.

The company manages 3.7B NOK under a mandate from the Norwegian Parliament (Stortinget) and invests on the same terms and conditions as private investors, with a clear exit strategy for all investments. 2B NOK were provided at inception and an allocation of an additional 1.5B NOK was agreed in 2011.

Investinor invests in highly competitive and promising Norwegian companies aiming for international growth and expansion within the following sectors: Cleantech, Aquaculture, Oil and Gas, Marine, Maritime, Travel, ICT and Lifescience.

Investinor is one of the major venture investment companies in Norway, both in terms of manpower and capital under management. The team is a value adding mixture of engineers and business professionals with industrial and entrepreneurial experience.

Investinor is an evergreen investor with a long-term perspective on ownership in portfolio companies. The company is financially strong and has a consistent, credible investment philosophy. It always co-invests with private players and has a co-investment strategy whereby it can take up to 49 % equity ownership of a portfolio company.

At the end of June, 2012, Investinor had a portfolio of 27 investments.

## **6.3. Experiences and current developments**

It has been suggested that a future wave of new seed funds should be made up of larger funds. This idea is in line with research findings and OECD studies demonstrating that funds with sufficient critical mass in terms of capital and organisation tend to perform better.

In 2012 Innovation Norway was requested by the Ministry of Trade and Industry to organise a new scheme of six national seed funds.

Some of the Government guidelines for the new funds are:

- The funds will invest in the seed and early stages with the opportunity to use the capital for internationalisation of and changes in the companies
- Average size of about 500M NOK and financed by equity with a 50/50 division between private and public funding.
- The setting up of the funds will be subject to the raising of sufficient private capital
- The Government will incentivise private investor involvement by paying a 15% higher price than private investors for the shares in the fund. This risk reduction function is needed to attract private investors. The life of the funds will be agreed in negotiation with private investors but limited to 15 years
- The funds will operate on commercial terms
- Innovation Norway will manage the Government's holdings in the funds
- The focus of the funds will depend on the competence of the management of each individual fund
- The intention is to establish funds all over Norway, with one fund in Northern Norway being mandatory
- The new funds will be set up gradually as private capital is raised
- New fund schemes must be approved by ESA, the EFTA surveillance authority.

Regarding EU policy, Innovation Norway stresses the importance of clearer EU-Commission guidelines for public investors on what is considered government support as well as commercial terms to enable public investors to design suitable set-ups and programmes.

As stated above, Investinor received additional capital following a decision made in 2011. During 2012 the board of Investinor decided to develop the organization by establishing a team for venture capital investments and another for the expansion stage to further strengthen investment operations and add specific competence for the expansion of existing and future portfolio companies.

# 7 Sweden – overview of direct public investors

## 7.1. Introduction to the Swedish market

The following text provides an overview of public investors in Sweden and the models they use. A brief description of current discussions regarding the organisation of public investors is included.

Sweden has a high ranking in terms of Innovation and R&D in various benchmarking reports and is also among the most highly ranked regarding the percentage of venture capital in comparison to Gross Domestic Product (GDP).

However, the Swedish venture capital market is currently under a great deal of pressure. It has undergone major changes in recent years that have seriously affected the number of new companies being funded by private VC firms. The risk aversion associated with early stage investments has increased due to the financial crisis.

The level of venture capital investments has been in decline in Sweden since 2009. The second quarter of 2012 is the weakest quarter since 2007 in terms of the number of investments and invested amount on the Swedish venture capital market. However during the first half of 2012 there have been positive signs in terms of fundraising and increasing interest from international investors. In total 932M SEK has been fundraised within venture capital, which is more than in 2010 and 2011 combined.

There has been a minor increase in the share of private investments on the Swedish venture capital market. During the last 12 months the share of private investments was up to 69%. The share of initial investments compared to follow on investments has gone up slightly.<sup>4</sup>

In recent years there has been a clear lack of private capital in the early stages. The government response to the financial gap in the early stages has been to increase funding of later early and expansion stages through the launch of Fouriertransform, Inlandsinnovation and ALMI Invest, which received funding from the EU Structural Funds, government agencies and regional players, all of which are described in more detail below.

4) Source: Swedish Private Equity & Venture Capital Association, SVCA

## 7.2 Direct public investors

Sweden has a number of direct public seed and VC investors set up for different purposes. Below is an overview of the main investors. There are ongoing discussions about potential mergers of public investors and a review of the entire system.

### **Industrifonden**

Industrifonden ([www.industrifonden.se](http://www.industrifonden.se)) is an independent evergreen fund set up by the Swedish government in 1979. Industrifonden manages a total of 3.8B SEK, of which 1.4B is invested in companies.

Revenues are returned to the business for new investment. Industrifonden has been involved in over 50 successful exits since 2000. Qlik Technologies Inc, sold in 2011 with an exit multiple of 40 is Industrifonden's best investment so far.

Industrifonden invests directly and indirectly in Swedish small and medium-sized growth companies, mainly in the form of equity capital. It also provides various types of loan and guarantee. New portfolio companies should have no more than 250 employees and a maximum of 400M SEK in sales. Most of Industrifonden's investments are syndications with other investors. In some cases, Industrifonden may be the sole investor.

The investment operations are divided into three different areas: Life Science, Technology and Industrial Growth.

### **Fouriertransform**

Fouriertransform ([www.fouriertransform.se](http://www.fouriertransform.se)) is a state-owned venture capital company founded in 2008 with a total capital of 3B SEK, the aim of which is to strengthen the international competitiveness of the Swedish automotive cluster on a commercial basis.

Fouriertransform's overall strategy is to invest capital in and be an active owner of automotive-related companies with innovative and commercially viable products and services. Fouriertransform is organised as a Swedish limited liability company wholly owned by the Swedish Government.

Fouriertransform plays an active role on the board of the companies in which it invests as well as through its network of contacts in industry, research and development.

Investment can be made in any part of the value chain, i.e., from materials, components, modules and systems, to products and aftermarket services, as well as in all phases - from early to mature. The projects must be connected with Sweden, i.e., production and/or development inside the country.

Individual investments should not exceed 5 % of Fouriertransform's total capital, i.e., 150M SEK. Maximum ownership is generally 49 %. Up to 30.06.2012 Fouriertransform had made 16 investments totalling 550M SEK and three early divestments of unsuccessful investments.

### **Inlandsinnovation**

Inlandsinnovation ([www.inlandsinnovation.se](http://www.inlandsinnovation.se)) is a state-owned VC company with the mission of developing the business community in the inland areas of northern Sweden comprising the counties of Norrbotten, Västerbotten, Jämtland, Västernorrland, Gävleborg, Dalarna and Värmland.

Inlandsinnovation was founded in 2010 with a capital of 2B SEK and invests directly and indirectly in companies and innovation projects. Up to 30.06.2012, the company had invested 45M SEK in five companies.

Investments can be made in all industries and stages. The main priority is equity investment, but the company also offers other financial solutions.

### **Innovationsbron**

Innovationsbron ([www.innovationsbron.se](http://www.innovationsbron.se)) is a State-owned investment company that identifies, develops and invests in promising companies with international growth potential. Its role is to complement the market and invest where the risk is high and capital scarce. In the very early stages of a business idea there is often a lack of customers and capital.

Through active ownership Innovationsbron assists entrepreneurs to overcome the risks inherent in the early growth phase. Since 1994 Innovationsbron has invested in more than 300 companies, at a present rate of about 30-40 new companies a year, making it Sweden's most active seed investor. For every SEK invested by Innovationsbron in new portfolio companies in 2011, private investors invested 2.5 SEK.

### **At the end of 2011 Innovationsbron had direct holdings in 160 companies**

Innovationbron runs a national Incubation programme called BIG Sweden. The incubators support entrepreneurs to develop their business. The financing of the Incubators is result-based, measured by the quality in their business development process and incubator company progress. Innovationsbron is represented all over Sweden with regional offices in seven locations.

### **SEF 1-3 – ERDF funds**

SEF is one of the funds with European Regional Development Fund, ERDF, support in Sweden. The SEF fund invests in Skåne and Blekinge regions.

SEF I is run by Innovationsbron as a project, with a total capital of 36M SEK for investment. According to the regulations, Innovationsbron can invest up to 1M EURO without private co-investments. 50% of the fund is financed by Innovationsbron and 50% by ERDF.

At the end of 2011, SEF I had invested 17.8M SEK, while business angels and institutional investors had invested a total of 53.4M SEK, in 14 companies.

SEF II and III, also known as Ssefond, is run by Innovationsbron and financed by Innovationsbron, the Skåne and Blekinge regions, Tillväxtverket (the Swedish Agency for Economic and Regional Growth) and ERDF.

The fund has 130M SEK under management and focuses on investments in companies that have developed beyond the very early seed stage. In most cases the companies have passed the seed stage and/or need a larger amount of capital at the start. Investments can vary between 2 and 20M SEK per company. At the end of 2011, 46.6M SEK had been invested in nine companies.

### **Almi Invest**

Almi Invest ([www.almiinvest.se](http://www.almiinvest.se)) is a State-owned venture capital company that invests in Swedish companies with scalable business models. Almi Invest was founded in 2009 by Almi Företagspartner together with regional investors. The company manages a total of 1B SEK. Half of the capital comes from the European Regional and Development Fund, ERDF, which accounts for an investment of 500M SEK. The other 50% comes from regional investors and Almi Företagspartner. Almi Invest is an Evergreen Fund. Almi Invest consists of seven, regionally based venture capital funds, all with local offices.

1. West Sweden (Västra Götaland, Halland and Värmland)
2. Småland and Öarna (Jönköping, Kronoberg, Kalmar and Gotland)
3. East Central Sweden (Uppsala, Västmanland, Örebro, Sörmland and Östergötland)
4. Stockholm
5. North Central Sweden (Gävleborg and Dalarna)
6. Central Norrland (Jämtland and Västernorrland)
7. Upper Norrland (Västerbotten and Norrbotten)

The initial investment is typically 2-4M SEK. During the lifetime of an investment, amounts of up to 10M SEK can be invested by Almi Invest. The funds always form a syndicate with an investment partner, which means that Almi Invest can acquire a maximum of 50% of the shares in a new issue or convertible bond.



### 7.3. Experiences and current developments

Several studies have been performed in Sweden by external advisors and government agencies on the overall organisation of Swedish public investors. McKinsey & Company delivered a report on direct public investors in August, 2011. The purpose of the report was to review the current organisation of direct public investors in Sweden and suggest changes to create a system that:

- Provides financing to companies in the early growth stage in a way that complements the market
- Provides long-term financial stability by limiting the need for additional capital to be added to the system
- Contributes to good financial returns, i.e., measurable financial results and/or public benefit.
- Maximises the effect for the “customers” i.e. the entrepreneur or the company, by allocating capital where it is most needed<sup>5</sup>

The report concludes that there is a fairly high supply of public capital for VC investments. However, it is hampered by inflexible mandates and restrictions with regard to industries and regions. At present, a relatively small portion of the capital is allocated to the very earliest stages.

Suggestions in the report include a loosening of mandates as well as the merger of several organisations deemed to be overlapping.

The government has since the McKinsey report was published stated that they would like to work towards a clearer structure, where venture capital investments in early stages are gathered in one organization and later stage venture capital investments are gathered in another organization.

In 2011 the Government decided to merge Innovationsbron and Almi for the purpose of extending the regional reach of Innovationsbron's offering to innovative companies as well as making savings by eliminating overlapping functions. The merger, which will involve transferring Innovationsbron shares to Almi, should be completed by the end of 2012. The new structure of Almi has not yet been made public.

The Government has also recommended greater coordination between Industrifonden and Fouriertransform for the purpose of increasing the output, resources and flexibility of the investment operations over time.

In the budget proposal for 2013 the Government has stated that it will start the work of expanding the mandate for the two investors Inlandsinnovation and Fouriertransform.

5) Översyn av statliga riskkapitalaktörer, August 2010, McKinsey & Company

For Inlandsinnovation the change will pertain to the geographical restriction and for Fouriertransform the change will be regarding the industry scope extending it beyond the automotive industry to also allow for other manufacturing industries.

The goal is a flexible public organisation that can follow the market and adjust its efforts to business cycle changes and industry developments.

# 8 Iceland – overview of direct public investors

## 8.1. Introduction to the Icelandic market

As Iceland emerges from the severe economic shock that hit the country in 2008, it is evident that export-driven technology companies must play a key role in the future economy of the country. Iceland's resilient and entrepreneurial business environment has helped the economy to adjust after the collapse of the financial sector. Iceland's economy is now out of the recession, with real GDP growth of 2.4% forecast by the Central Bank of Iceland for 2012.

The seed and venture sectors of the economy have thrived in the aftermath of the crisis. A number of private and publicly sponsored incubators as well as accelerators have been set up in recent years. Initiatives include Start-Up Reykjavik (Tech Stars), and Klak accelerator. Deal flow is good and there is a clear movement of talent from the financial sector to the start-up arena. Angel Investment is growing and estimated at 10M EURO in 2011. At present, Iceland has three active stage and seed investment funds:

- Government sponsored NSA Ventures is an evergreen fund established in 1997. (see below)
- Frumtak, which is funded by NSA Ventures (40%) as well as private LPs, was founded in 2008. It is a closed end venture/growth fund that currently has a portfolio of 13 companies.
- Eyrir Sprotar is a privately held fund started by Eyrir Invest in 2012. Eyrir Invest has been a cornerstone investor in two of Iceland's flagship innovation companies, Marel and Össur. Eyrir Sprotar focuses on supporting ventures that have the potential for international growth and value creation, fully in line with Eyrir's "buy and build philosophy". Eyrir Sprotar currently has a portfolio of 2 companies.

The Bru II and Auður 1 funds are fully invested at present.

It is estimated that 20M EURO was invested annually in seed and early stage companies in Iceland in 2010 and 2011. However, a concern is that there will be an imminent lack of funding in Iceland, as closed-end funds are fully invested and have not raised new seed/early stage funds.

As noted in a recent report by McKinsey Scandinavia:

„Given the premise that Iceland should expect to be a developer of early stage companies, it also needs to allocate a disproportionate amount of investments to venture capital. Developing further access to growth capital and management support for early stage companies should therefore be a priority. ....On top of this, improved access to international venture capital markets should be a priority.”<sup>6</sup>

There are several challenges for the Icelandic venture environment, including:

- The size of the country makes it difficult to ensure a minimum viable fund size while at the same time making certain that there are sufficient funds
- The lack of experienced LPs in Iceland. Iceland has a relatively large and well-funded pension fund system; however, to date, pension fund activity in the venture capital market has been limited. This presents an obvious opportunity to change the situation and involve the pension funds to a greater extent in the future.
- Scaling Icelandic start-up companies. Given the size of the country it can be challenging to grow large companies from Iceland. Access to human resources as well as geographic distance from overseas markets can limit company growth. However, there are a number of successful growth companies that have been able to keep their headquarters in Iceland while establishing substantial sales offices or development and manufacturing operations in key international markets. Iceland needs to maintain a business/tax environment where fast growing start-ups are encouraged to keep a presence in Iceland while investing in international employees and operations.
- Exits. Icelandic trade sales are almost non-existent. Companies are reluctant to list on First North. The Icelandic stock market was nearly wiped out during the financial crisis and it takes time to regain the trust of investors. However, the country's largest companies are slowly returning to the market. Recent exits have almost exclusively been international trade sales.
- Attracting international LP investors. At present there are no international LPs investing in Icelandic managed funds. Attracting experienced international limited partners into well-managed Icelandic funds would not only help to attract local LPs but could also facilitate local funds to build international operations.

6) Charting a Growth Path for Iceland. McKinsey Scandinavia – Autumn 2012, p 88

## 8.2. Direct Public Investors

NSA Ventures ([www.nsaventures.is](http://www.nsaventures.is); formally the New Business Venture Fund) is the only public sector venture investor in Iceland and was set up in 1997 as a direct as well as a fund-of-funds investor. Currently, the organisation has a portfolio of 39 Icelandic companies and 3 fund investments (Bru, Audur, Frumtak). It has a fund size of 32M EURO and invests approximately five million Euro annually. The fund has had several successful exits in the last two years with returns ranging from 2x to 8x, which means that it has been able to continue investing. It is not mandatory for the fund to work with private sector investors, although whenever possible it attempts to find private sector co-investors.

## 8.3. Experiences and current developments

The structure of NSA Ventures is currently under review. A Government working group has been set up to examine the legislation and operations of the fund and evaluate how NSA Ventures can collaborate more closely with potential LPs, such as pension funds, in order to increase the total amount of capital available for start-ups.

## 9 Estonia and the other Baltic States – overview of direct public investors

### 9.1. Introduction to the Estonian and Baltic markets

Below follows a brief description of the status of and major challenges facing the Estonian and Baltic VC and early stage markets.

The early bird in providing venture capital was the Baltic Small Equity Fund, founded in 1997. It financed start-up companies in the Baltic states and has now fully divested its portfolio companies. It was mainly financed by the EBRD (European Bank for Reconstruction and Development) with a committed capital of 10.7M USD. In 2004, when work began on designing and developing the EDF (Estonian Development Fund) model, venture capital investments in Estonia were so low that they fell below the 'radar screen' of VC statistics.

Since 2007, the early stage market situation has improved significantly. As well as the publicly financed EDF, a number of business angels or their investment companies (e.g. Ambient Sound Investments) provide capital for local start-ups. In addition to Estonian investors, Scandinavian – mainly Finnish – investors have started to follow and invest in Estonian start-up companies. For example, Conor Venture Partners has invested in Crystalsol (new type of flexible photovoltaic technology) and Aura Capital in Fromdistance (device management technology).

Currently the EstVCA (Estonian Venture Capital Association) has 18 full members, comprising traditional VC funds, business angels, pension funds, etc. The first investments by current EstVCA members were made in 2002. In the period 2002-2010, 70 out of a total of 120 investments in Estonian companies were made by EstVCA members. Of these 70 investments, 14% went to seed and 30% to start-up stage companies. There are a couple of funds (e.g. managed by Baltcap) that invest in later stage companies. The number of early stage investments increased significantly after the Estonian Development Fund became involved.

According to the EVCA (European Private Equity and Venture Capital Association), about 329M EUR was invested in 91 companies in all stages of private equity in the three Baltic States between 2007 and 2010, which is only a fraction of the total investments in

the CEE region. However, only 13 of the EstVCA members issue reports and the figures mentioned above include expansion and buy-out stage investments.

In general, the main problems experienced by Estonian investors are limited funds for follow-up investments (e.g. only 4 investors out of the 18 members of EstVCA invest actively) and insufficient international networking for developing globally competitive portfolio companies and securing subsequent financing rounds.

According to the “Early-stage Investment by the Estonian Development Fund” study by the University of Sussex and Technopolis Group in 2010, hereafter termed the “EDF study”, a funding gap in the range of 10K-100K EUR still exists in Estonia. The number of business angels and seed investments is quite low, as investors’ risk-bearing capacity as well as knowledge of seed investing is fairly poor.

Estonia has been a starting-point for several high-growth technology companies, such as Skype, Erply (point of sale software and inventory system), CrabCAD (environment for CAD-engineers, designers and manufacturers) and Fits.me (real-view solution for online shopping). However, in addition to market failure in private equity supply, there have been problems on the demand side. The expected number of new, technology-based, high added-value businesses has not materialised. Only about 30-40 high-growth companies are created annually, of which 10-15 are able to raise funds and 6-8 manage to become internationally successful.

## 9.2. Direct public investors

Short description of the major public investors in Estonia and if relevant in the other Baltic states.

### **Estonia**

To overcome market failure in early stage equity financing, the Estonian Development Fund (EDF; [www.arangufond.ee](http://www.arangufond.ee)) was established in 2007 as an independent public legal entity by the Estonian Parliament. Today, it is the only source of public funding for equity investments available to local companies. The first investment was made in May 2008 and currently the portfolio contains 15 enterprises. The EDF mainly invests in high-growth start-up companies without restrictions on activities or sectors (other than EU guidelines). The planned investment period is 5 years and investments generally range from 100 to 500K EUR per company, with a maximum limit of 3M EUR per company. So far, the fund has invested 6.6M EUR. The EDF takes 10-49% of ownership and all investments must be made together with an independent private sector co-investor on identical terms. Besides direct investments in equity, the EDF can also provide convertible loans.

Final investment decisions are made by the Fund's management, but the deals are first presented to the advisory board known as the Expert Committee, which consists of industry experts with international business experience. Seed stage investments of less than 300K EUR are not required to be presented to the Expert Committee. After investment the EDF plays an active role on the Supervisory Board of the company in which it has invested.

The EDF regulations also allow investment in fund-of-funds, but no such investments have been made to date due to the lack of suitable early stage funds. EDF has made one successful partial exit (part of the business was sold). Further exits are expected starting in 2012.

At present, the EDF is in the process of applying for a fund manager licence and preparing a new subsidiary fund (Early Fund II) with the first closing of 12.8M EUR to be invested in 2012-2013.

### **Latvia**

According to the survey conducted by the TeliaSonera Institute at the Stockholm School of Economics in Riga (Oct, 2010), there were 13 PE/VC firms in Latvia as of June 2008. Only funds fully or partially financed by the State (such as UAF, MVKAF, Second Eko Fund managed by AS "Eko Investors", ZGI fund managed by SIA "Za s gaismas invest cijas", TechVentures by SIA "TechVentures Fondu Vad bas Komp nija) invest in start-up companies. As a rule, these funds make investments of up to 200K EUR.

Three funds with a total capitalisation of 32.1M EUR were created in December, 2006, targeting early stage companies and SMEs with growth potential, and about 50% of the capital was raised from the private sector. In this context, it should be stressed that public funding is subordinate to private investment and acts as downside protection with restricted profit interest. Thus the aim is not to crowd out private investment. Fund management companies were selected through an international open tender procedure.

The programme had a short life-cycle of 2-3 years. The reason for creating three funds rather than one larger fund was twofold. First, there was a desire to promote competition in the venture capital market and second, training three teams was considered favourable as it would provide more people with experience of fund management. However, in retrospect it is considered that to be sustainable and successful, funds need a critical mass in order to be able to employ a truly professional team with adequate incentives and have sufficient funds for follow-on investments.



There are 2 JEREMIE funds in Latvia, established in 2010. One of them – SIA Imprimatur Capital – also invests in seed and start-up funds (total capital of approx. 12M EUR, of which 10M is in a VC fund and 2M in a seed fund as of March 2011). The other JEREMIE fund is managed by Baltcap (assets under management are 30M EUR, of which 20M is from the public and 10M from the private sector).

### **Lithuania**

There are 3 JEREMIE funds operated in Lithuania by LitCapital (70% public money), Baltcap (70% public money) and Angel Fund 1 (100% public money). Angel Fund 1 (8M EUR) invests in start ups and early stage companies. The maximum investment is 250K EUR together with angel co-investors (max 250K EUR). LC and BC invest up to 3M EUR in expansion/growth (20M EUR per fund). AF has 6-7 investments, while LC and BC each have 2 investments so far. All funds started in mid 2010.

There is a fourth JEREMIE fund in preparation (70-100% public money). It will consist of 2 parts – early stage and growth/expansion. The total fund is expected to be 15-17M EUR.

To overcome the gap in financing the proof-of-concept and commercialisation stages of Lithuanian technology innovations spinning off from Universities, Research Centres and R&D based companies, the Ministry of Economy plans to launch an additional fund, most probably administered by the local public institution INVEGA (currently providing state guarantees). At present, two options (1 or 2 funds- seed and start-up) are under discussion, although no decision has been made about structure, size, etc.

## **9.3. Experiences and current developments**

Comments on which models have been successful and which have not.

Taking into account the short existence of EDF in Estonia, the main challenges are insufficient deal flow and difficulty finding co-investors. By law, EDF is legally obliged to find co-investors to invest at exactly the same conditions in each deal. There are several positive outcomes of such a system – proof that all investments are made under market conditions, extra know-how, not crowding-out private capital, less time spent on negotiations. Nevertheless, the process of finding co-investor(s) can be very time-consuming and some deals have not been closed due to the lack of co-investors. This was a more significant problem in EDF's first year of investment activities.

Today, the EDF has no problem finding co-investors, although there are cases where existing co-investors are unable to participate in follow-on investments. Currently, the EDF intends to gather potential business angels into a separate fund to develop the venture capital market in Estonia in the hope that the financing possibilities for early stage enterprises will improve. The angel fund will also make investments together with the EDF. The latter is restricted to only investing in Estonian-registered companies,

which severely limits the pipeline as the country is small. Despite a recent boom of technology start ups in Estonia, finding quality investment targets is still a struggle. The fund often actively works with potential investment targets for many months in order to help the enterprises become “investable”.

The EDF's main success factor has been the decision-making process, which is totally non-political. Deals are not introduced nor decisions made by the Supervisory Board, which is made up of politicians, who are awarded seats due to their position, e.g vice-chancellors of the universities, ministers etc. This allows decisions to be made relatively quickly with no political influence. The Expert Committee has also proved to be an excellent place to obtain industry insights and valuable business advice. Last year the EDF introduced a two-step Expert Committee system. In addition to presenting the deals to the Committee before the final decision, projects are introduced to its members at an early stage in order to obtain their advice and feedback in preparation for the investment decision.

The study concludes that without EDF support it would be extremely difficult for Estonian companies to obtain funding. It also highlighted the fact that the co-investment model was working well and supported a shift to a more international outlook in terms of the Fund's activities and the move towards a single Baltic VC market with an international focus. It emphasised the role played by the fund in cooperating with foreign VC funds, acting as a “landing partner” and creating a business-friendly environment for them to work in.

The Estonian ecosystem has a number of positive (no tax on reinvested profits, easy to set up a company, etc.) and negative elements. On the negative side, some VC investment tools such as convertible loans (which is deemed debt rather than equity) and preferred stock are difficult or impossible to use.

Estonia has considerable potential to attract foreign early stage technology-based firms due to lower costs, sophisticated R&D support and the ability to exploit EU Structural Funds. The EDF study made several suggestions for future developments, among others, the advice to capitalise the fund adequately (in line with international experience, “adequate” is at least 30MEUR), consider specific forms of support for “young innovative enterprises” and improve the taxation and social security environment. In addition, drawing on experience from other countries, additional funding in the range of 10 - 100K EUR invested through the EDF for proof of concept, prototype and international market entry testing could be considered. It also strongly recommended not to multiply initiatives and that any future seed capital fund or support for business angels' professional development and syndication should be managed as part of the EDF's activities and not as separate initiatives.

An extensive grant programme is available to Estonian enterprises in order to increase financing possibilities for SMEs and also improve the companies' quality. Most grants are designated for ventures in the pre-seed and seed phases - for example start-up, development and product development grants followed by export marketing grants later in the enterprise's life cycle. Several other programmes and soft activities also support growing enterprises. Start-up loans, business loan guarantees and technology loans are other options for developing businesses. The EDF itself started several initiatives for promoting venture capital and start-up entrepreneurship between 2008 and 2010 (virtual business incubator SeedBooster, EstVCA, VentureLab, etc).

Similar supportive instruments exist in other Baltic States. The Estonian government decided to support the Estonian start-up ecosystem development by creating a special programme known as "Start-up Estonia". The programme has a budget of 2.2M EUR until the end of 2013. The board is presently validating the activities of a start-up accelerator in order to support local start-ups.

In the autumn of 2012 the European Investment Fund, EIF, launched a Baltic Innovation Fund. The Baltic Innovation Fund will invest 100M EUR into private equity and venture capital funds focused on the Baltic States over the next four years through a 'fund of funds' process to further developing equity investment into small and medium sized enterprises (SMEs) to boost growth.

# 10 Scotland – overview of direct public investors

## 10.1. Introduction to the Scottish market

The Scottish VC and early stage market is segmented with an expansion capital market characterized by VC investment in existing portfolio companies, and a start-up and expansion risk capital market characterized in the main by business angel syndicates investing in new and expanding companies.

Annual market activity in the region of 120M GBP invested in approximately 150 companies, of which around 70M GBP is invested in deals of 2 M GBP or over. The three sectors that consistently secure the most investment are ICT (software, IT, Internet, telecom), life sciences (medical, healthcare, pharmaceutical, biotechnology) and energy (marine, wind).

There has been a significant and deliberate policy shift away from individual business angel investors to a more formally organised market, which has grown from just 2 syndicates in 2001 to 19 in 2011. This growth is largely attributed to the Scottish Investment Bank's role in funding LINC Scotland to form and develop new syndicates, combined with the introduction of co-Investment funds designed with the specific remit of facilitating the development of the angel syndicate market in Scotland. In particular, the Scottish Co-investment Fund has allowed business angel syndicates to make more and larger investments, as well as following on their investments in subsequent rounds, thereby filling at least part of the gap left by the withdrawal of formal venture capital from the lower end of the risk capital market.

Business angel syndicates have adopted a 'cradle to exit' investment model, committing themselves to investment in the range of 1M to 2.5M GBP with the intention of seeing through the realisation of the growth potential of their portfolio companies. Consequently, established angel investors operating through syndicates have been increasingly concentrating on investing larger amounts in follow-on investments in their portfolio companies. On the other hand, investing in start-ups has to a large extent been the preserve of individual angels and angel syndicates entering the market for the first time with new funds to invest.

**Major challenges:**

- Under current market conditions, a continual flow of new investors will be needed to maintain the capacity to invest in high-growth potential start-up and early stage ventures;
- Lack of exit opportunities for established investors;
- Concentration on servicing existing portfolios;
- Investor ‘fatigue’;
- The need for greater complementarity between institutional investors and business angel investors;
- The separation of the angel and VC markets may significantly limit the realisation of the growth potential of seed and early stage companies;
- The level of investment needed to commercialise opportunities in certain sectors, e.g., renewable energy, pharmaceuticals;
- Recapitalizing public funds in a challenging fiscal environment.

## 10.2. Direct Public Investors

Scotland’s most active early stage investor is the Scottish Investment Bank (SIB; [www.scottish-enterprise.com](http://www.scottish-enterprise.com)), which invests between 20M and 30M GBP in approximately 100 companies per annum. SIB is a division of Scottish Enterprise, the Government’s main economic development agency in Scotland. SIB manages 3 early stage co-investment funds with capital under management of 115M GBP as well as being the cornerstone investor in a fourth, a 94M GBP mezzanine fund managed by a Scottish private sector fund manager. In addition to its capitalized funds, SIB invests approx. 4M GBP per annum directly from its balance sheet. The European Regional and Development Fund is an integral part of SIB’s main funds, accounting for 40% of each fund’s capital value. SIB participates in approximately two thirds of all early stage deals annually, investing a fifth of the total funding and thus serving as a significant catalyst to the market.

Scotland’s most active early stage private sector investors include: Archangel (angel syndicate), TriCap (angel syndicate), Barwell (family office), Highland Venture Capital (angel syndicate), Braveheart (investment management company), Souter Investments (family office), Sigma Technology Management (VC), Par Equity (VC), Pentech Ventures (VC) and Scottish and Southern Energy (corporate investor). Approximately 60% of early stage private sector investment activity in Scotland is accounted for by local angel syndicates; the remaining 40% is made up of family offices and early stage VC as well as corporate investors, both local and international.

Archangel Informal Investments is Scotland’s leading business angel syndicate with over 100 members, investment of approx. 10M GBP annually and a portfolio of 29 companies.

Braveheart Investment Group has developed from an informal angel syndicate to an investment management company that has completed 100 deals in its 14 year history and currently has a portfolio of 27 companies. TriCap - since its launch in 2004 this business angel syndicate has completed deals valued at 34M GBP and has a current portfolio of 20 companies. Highland Venture Capital is an angel syndicate formed in 2006 to invest in growing and start-up businesses.

Souter Investments is the private investment office of Brian Souter, founder of Stagecoach, and has a portfolio of 120 investments valued in excess of 400M GBP. Sigma Technology Management Limited is the fund manager of Sigma Capital's four venture capital funds with offices in Edinburgh and London. SET Venture Partners is the Dutch-based management company of the Sustainable Energy Technology Fund, one of Europe's leading Cleantech Venture Capital Investors.

#### **Examples of public investment models**

Scottish Enterprise (SE; [www.scottish-enterprise.com](http://www.scottish-enterprise.com)) has been investing in the early stage risk capital market since the organisation was founded in 1991. Initial efforts were focused on direct funding, through the creation of a directly funded, public sector managed VC fund (Scottish Development Finance) within the regional development agency as one of its core services since its inception in 1991. More recently (2002 to the present), the policy focus has shifted to Scottish Investment Bank support for private sector investors through co-investment funds (and in particular the Scottish Co-investment Fund), which demonstrates how public sector interests and private sector expertise and standards can be effectively combined.

Unlike a standard VC fund or business angel investor, the Scottish Co-investment Fund (SCF) does not find and negotiate deals on its own. Instead, it forms contractual partnerships with private sector business angel syndicates, VC and corporate investors. These partners find the opportunity, undertake the due diligence, negotiate the terms of the deal and commit their own resources to the equity investment. If the opportunity requires more investment than the partner can provide, it can request the SCF to co-invest directly into the opportunity, alongside on equal terms. The private sector Partner determines how much the SCF can invest in a deal, as according to the terms and conditions for the operation of the Fund (governed by state aid rules and the conditions associated with ERDF funding), the SCF cannot invest more than the private sector partner. Companies seeking investment approach partners directly. The SCF has no influence whatsoever in the investment decision-making process, which is delegated to the private partner.

The design of the SCF, with the fund as a *pari passu* investor alongside private sector investors, has had a number of key impacts on the early stage risk capital market in Scotland:

- **Leverage** - the SCF has leveraged additional funds into deals, with the leverage rate approximately 1:2 compared to an anticipated rate of 1:1 at fund inception;
- **Speed** - the design of the SCF ensures that investment decisions are taken by private investors, with the Fund decision to co-invest being conveyed in the form of a quick assurance that up to 50% of the funds needed to complete an investment will be made available for eligible deals;
- **Design** - the SCF is dominated by business angel syndicate partners, who are the dominant players in the early stage capital market. The availability of the SCF addresses liquidity and investment appetite issues for syndicates that need to provide follow-on funding for their portfolio companies after the withdrawal of VC investors from the market in Scotland;
- **Deal size** - the support of the SCF allows investors to consider larger deals and commit to follow-on deals to a greater extent than their liquidity and investment preferences would otherwise allow, making it possible for companies to raise all the capital they require;
- **Leverage and syndication** - the SCF has successfully leveraged additional investment from private sector investors in addition to that from partners, thus providing clear evidence of increased syndication in a maturing Scottish early stage risk capital market;
- **Additionality** - in providing additional investment liquidity for partners, the SCF helps to extend the funding pipeline rather than replacing existing investment: the annual reviews of the risk capital market in Scotland reveal that it has separated into two distinct parts, dominated by business angel investors on the one hand (supplemented by a small number of early stage institutional VC funds) and, on the other, VC investors interested in much larger deals, where the SCF plays an increasingly important role in the development of ventures that would otherwise struggle to attract institutional VC.

This design avoids the common problems of public sector intervention in venture capital markets, in that it removes the public sector from decision-making and fund management processes, relying instead on the private sector to make all investment decisions. It avoids introducing distortion into the market, assuming the position of a *pari passu* rather than a subordinate investor, thus accepting lower or capped returns and covering the first loss on erosion of fund capital. As such, the SCF fund design offers the prospect of mobilising investment capital within a regional economy from existing investors by 1) enabling them to make more and larger deals, 2) attracting investment capital from investors outside the region, and 3) addressing one of the limitations of regional economies with weak indigenous VC markets in a manner that minimizes the cost to the public purse and the risk to public funds.

### 10.3. Experiences and current developments

Scottish Government and Scottish Enterprise policy towards developing the early stage investment market continues to be one of regular and detailed market analyses (including consultation) to ensure that the existing co-investment funds continue to achieve their market catalyst objectives; identify new market failures and, where appropriate, address them by introducing new funds.

The effectiveness of supply-side interventions can be compromised unless efforts are made to address failure in the demand for investment. Consequently, an integral part of Scottish Government and Scottish Enterprise policy for developing the early stage market is the provision of financial and investment readiness information to companies through a network of public and private sector advisers.



# 11 Germany – overview of direct public investors

## 11.1. Introduction to the German market

Below is an introduction to the status of and major challenges facing the German VC and early stage market.

The 2010 annual report of the German Private Equity and Venture Capital Association e.V. (BVK, [www.bvkap.de](http://www.bvkap.de)) revealed that the number of members investing in PE (including VC) had increased to 218. An estimated 40 additional companies exist alongside the BVK. The members of the BVK employed about 1,900 persons (of whom 1,190 were professionals) and received approximately 42,300 capital enquiries compared to 38,400 in 2009.

The German PE/VC fundraising amounted to 927M EUR, a decline of 13 % compared to 2009 (1.071M EUR) and the same level as 1996. Only a few new funds were closed. About one third was destined for mostly later stage Venture Capital. The seed as well as the bordering start up-phase lacks private capital – public funds such as High-Tech Gründerfonds, Bonn (all over Germany) and regional funds such as Seedfonds Bayern (managed by Bayern Kapital) are all attempting to close the gap as much as possible.

How to increase fundraising is one of the main topics within the industry, including e.g. the introduction of a guarantee programme in favour of fund investors.

German PE and VC funds invest approximately 3.115M EUR in Germany and around 911M EUR elsewhere.

In 2010 Venture Capital Investments totalled about 650M EUR (similar to 2009). Within the VC-sector, seed and start-up investments dropped by 11 % to 367M EUR, while later stage VC investments grew by nearly a quarter to 288M EUR. The exit situation had a slightly positive trend.

In the first half of 2011, Venture Capital Investments totalled 325M EUR (similar to 2010). Seed and start up amounted to 190M EUR and later stage VC about 135M EUR, thus there was little progress in terms of the funding of young companies.

When broken down into regions, the highest level of investment in 2010 took place in Bavaria (25 %), Baden-Württemberg (23 %) and Berlin (18 %), while investment in the other federal states was considerably lower. 83 % of the financed companies employed less than 100 people. 17 % of the investments were in companies with revenues of less than 50M EUR and 32 % in companies with 50 to 250M EUR.

In addition to the preceding topics, the major issues facing the German PE/VC sector are the need for an improved fiscal framework (e.g. removal of the sales tax on management fees payable by a fund to its management company, clear and firm rules for fund investors), a comprehensive private equity law (including VC), the of the AIFM-guidelines into national law as well as the new European regulations for Venture Capital (may be linked with the PE law) presently under discussion.

## 11.2. Direct public investors

Because of the lack of private investors in the seed phase, some public funds use a "Coach-model". The investment is made by appointing a business coach, who checks and prepares the documents concerning the application for seed fund participation, provides technical and operational advice as well as comprehensive support in the early stage of the project, monitors the use of seed money and plays an active role in the transition to other forms of financing. Thus in addition to seed funds, the young company obtains access to the business coach's entrepreneurial know how and network.

The largest fund of that kind is the High-Tech Gründerfonds ([www.high-tech-gruenderfonds.de](http://www.high-tech-gruenderfonds.de)) in Bonn (founded in 2005) with a managed capital of 272M EUR. A smaller part of the capital was invested by big companies such as BASF, Siemens, Bosch, Daimler, Telekom and Zeiss. The fund invests all over Germany and in special cases also pari passu to private investors. In addition, there are some regional funds such as Seedfonds Bayern (established in 2003, approx. 20M EUR, 2. tranche since 2010: 24M EUR).

There are some funds, mainly in the assisted areas of eastern Germany, which do not have a private partner in the start-up phase, because it is especially difficult to find such a partner in these regions.

In North Rhine-Westphalia, the NRW Bank created a fund-of-funds model (30M EUR) in 2005. Seven regional seed funds were created in a roughly 50/50 partnership with experienced regional partners (mostly banks).

Generally beginning in the start-up phase (as mentioned above there are often no private partners) co-investment funds follow the lead-investor-model:

The co-operating lead investor (investment company or Business Angel) also invests in the project. The capital of the public fund must be below or equal to the private capital - up to 70% of public capital is permitted in assisted areas with special approval from the EU-Commission or for other special reasons. If the conditions differ from *pari state aid* is provided, which has to be approved by the EU-Commission. The aforementioned EU-commission approval is normally granted to the fund-structure depart from individual investment.

The lead-investor (whose excellence in technical and management know-how must be proven) supports a technology company comprehensively for example in questions of strategy and its realisation. The investor uses network contacts particularly with regard to identifying potential customers and partners. A common exit for private and public investors is planned.

Since 2004, the biggest co-investment fund in Germany, i.e. the ERP-Startfonds managed by the KfW Frankfurt/Bonn, in cooperation with the German Ministry of economics, is pursuing similar programmes. The third tranche started in 2011 and contains 250M EUR; In the first two tranches, 821 contracts were closed worth 380M EUR. The applicant must be a small young enterprise in accordance with the rules of the EU-COM. The maximum amount of capital is 5M EUR and the conditions are *pari passu*.

In some regions of Germany there are public co-investment funds, for example since December 1995 in Bavaria, managed by Bayern Kapital ([www.bayernkapital.de](http://www.bayernkapital.de)). These funds are -including a special EFRE fund-of-funds totalling about 50M EUR. The maximum amount paid to one company is 2M EUR, conditions are *pari passu* or with special EU-Commission approved state aid.

### 11.3. Experiences and current developments

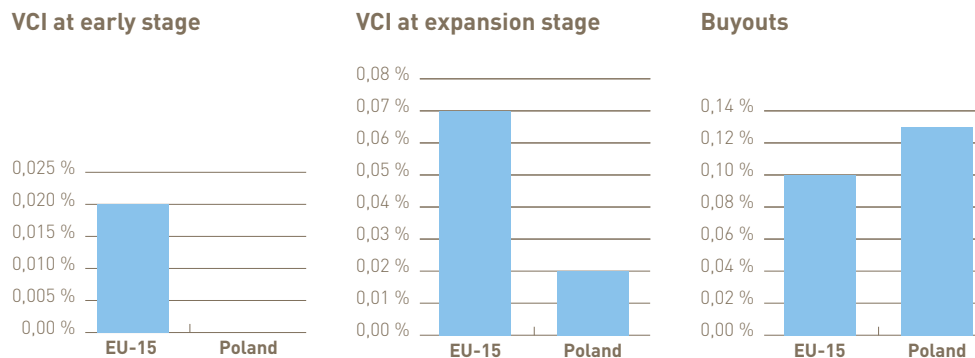
The success of the above mentioned model depends on the availability of cooperating private investors - especially in the seed phase where there is a great shortage.

# 12 Poland overview of direct public investors

## 12.1. Introduction to the Polish market

The Polish venture capital market is relatively under-developed. According to the Eurostat “Science, technology and innovation in Europe” report (2011 edition, data from 2009), Poland has the lowest rate of early stage investment to GDP (Gross Domestic Product) of all EU-member states and less than a third of the EU average for expansion VC investment. In contrast, the Polish buy-out market is fairly strong, as the value of transactions to GDP is 30% higher than the EU average. These statistics are presented in the chart below:

**Figure 1: Private Equity (PE) and Venture Capital Investment (VCI) in Poland compared to the EU average (as % of GDP)**



Source: Eurostat: Science, Technology and Innovation in Europe 2011.

Since the start of the transformation from a centrally planned to a market economy in the early 1990s, policy makers and especially their foreign advisors have been aware of Polish enterprises' need for smart capital. The first initiative was the 240 million USD Polish-American Enterprise Fund established by the U.S. Government in May, 1990. This fund invested in over 50 enterprises, created a system of micro-loans and established the Educational Enterprise Foundation, all of which has had a long-term impact. In 1992 Enterprise Investors (EI) was established as a fully private general partner (GP) for the

Polish-American Enterprise Fund. EI became one of the most successful GPs in Europe and raised the next seven funds with a total capital of 1.7B EUR, which was invested in 90 companies with an average return of almost 3 times money. Enterprise Investors and other private equity funds (e.g. Inova Capital) attracted global players and the Polish PE market has been developing quite rapidly.

Unlike the PE market, Seed and VC remained under-developed. There were initiatives based on both public (e.g. seed funds sponsored by the British Know-how Fund) and private capital (e.g. MCI Management listed as a VC fund manager). The Polish VC market suffers from lack of global success stories and an under-developed VC ecosystem. Both local and global institutional investors avoided this asset class. The few active fund managers that existed constantly moved away from the early stage towards larger deals and even the most successful changed their strategy to become small or mid-cap private equity firms.

## 12.2. Direct public investors

About 10 years ago, it became clear that “the invisible hand of the market” would not solve the challenges of the Polish VC market. Entrepreneurs perceived access to capital as the major constraint for the development of their companies. The situation was particularly difficult for early stage, small and medium sized enterprises (SMEs). The policy makers decided on quite a sophisticated solution. In 2005, the National Capital Fund (KFK; [www.kfk.org.pl](http://www.kfk.org.pl)) was created with the mission to improve access to capital for SMEs. KFK fulfils this mission by investing public money along with private in VC funds managed by private GPs and attracts private capital by reducing the risk for private partners. KFK is an evergreen fund so the GPs anticipate a long- term relationship.

In 2006 (before the KFK was fully operational), EU Structural Funds were allocated to seed funds. Combined with private capital, these funds enabled the creation of 6 seed funds that invested in 47 early stage companies. The total invested capital was in excess of 25M EUR.

In 2007, the KFK started investing in seed and VC funds. As of Q3 2011, the KFK had committed about 100M EUR to 11 funds and another 120M EUR will be invested until the end of 2012. Total capitalization of the funds will be at least 400M EUR.

In summary: for many years Polish entrepreneurs had very limited access to capital. Since 2006, availability of equity for early stage enterprises has been gradually improving. Now that capital is available, a new challenge might be the relatively few attractive investment opportunities. With strong private and public capital markets, the exit from good projects should not pose a major challenge.

### 12.3. Experiences and current developments

Although no public direct investors fully fall under the definition set out in this Initiative, there are several other schemes to facilitate equity investment in early stage companies. The institutions can be grouped into four categories:

1. Government sponsored venture capital funds (GVC)
2. Government sponsored seed funds / incubators (GSC)
3. Publicly supported business angel networks (BAN)
4. Guarantee/loan providers (DEBT)

Large scale Government involvement in venture and seed capital is a fairly new phenomenon in Poland and too early to evaluate. At this stage it would be fair to say that access to capital for companies in the early stage has improved dramatically in recent years. GSC funds and incubators are competing for promising projects and offering innovators excellent investment terms. A similar process can be observed in the case of GVC. More and more funds are being created and tough competition is expected between them. A parallel system of guarantees and loans for SMEs has also been developed. Absorption of DEBT instruments is not as strong due to the reluctance of Polish SMEs to accept financial leverage. The attractive terms offered by the Government-supported DEBT might create increased interest in financial instruments.

In the last 20 years, the equity gap in Poland was to some extent mitigated by individual private investors, the so-called business angels, who started to create formal and informal networks in the late 1990s. Present initiatives for the professionalization of BANs have contributed to a more structured approach to business angel investment.

Current discussion on financial instruments for early stage companies is focused on two issues: more direct involvement of public investors, e.g. a co-investment scheme with business angels/GVC/GSC, and the proportion of national and regional programmes.

The KFK public policy recommendations are three-dimensional. Firstly, more focus on equity instruments. Financial leverage means more risk and SMEs should not have to shoulder too much. Secondly, the KFK strongly believes in public-private partnership but that more direct involvement from public investors should be facilitated. The new KFK strategy (under development) assumes that in addition to being a fund-of-funds, the KFK will co-invest directly in the companies. Thirdly, capital providers should be geographically close to their targets. This is especially true for early stage companies that require constant monitoring and coaching.

# Table of abstract


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This report has a dual content. It first describes joint policy advice presented by the Nordic-European Public Investor Initiative members to the EU Commission regarding structural fund regulations for the 2014–2020 programming period. Secondly, the report includes brief descriptions of existing programmes and models used in the different European countries in which the member organisations are based.

The Nordic-European Public Investor Initiative fulfils a dual purpose. First, it strengthens the effect of public investment in venture capital by a greater level of interaction and cooperation as well as experience sharing between Nordic and other European direct public investors. Second, it influences the EU decision-making process to make well-informed design of new programmes and initiatives.

The Initiative comprises a network of 11 national public investors in the field of seed capital and venture capital with 3.2B EURO under management and more than 1,600 portfolio companies as well as the European Investment Fund. The Initiative members are drawn from 8 northern European countries.

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# Nordic-European Public Investor Initiative

Experience sharing & Joint advice on EU policy  
*November 2012*

The European venture capital market is under severe pressure. European countries have implemented and are planning further large-scale initiatives to ease the situation, which would otherwise have major implications for promising European high growth companies.

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## **Owner of the Initiative:**

Nordic Innovation

## **Members of the Initiative**

Finnvera, Finland

Finnish Industry Investment, Finland

Innovation Norway, Norway

Investinor, Norway

Innovationsbron, Sweden

Industrifonden, Sweden

NSA Ventures, Iceland

Estonian Development Fund, Estonia

Scottish Enterprise, Scotland

Bayern Kapital, Germany

Krajowy Fundusz Kapitałowy, Poland

## **Associate member of the Initiative**

European Investment Fund, EIF

## **Coordinator of the Initiative**

Nordic Investment Solutions

Nordic Innovation is an institution under Nordic Council of Ministers that facilitates sustainable growth in the Nordic region. Our mission is to orchestrate increased value creation through international cooperation.

**We stimulate innovation, remove barriers and build relations through Nordic cooperation**

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