Inovační centrum Ústeckého kraje
Velká Hradební 2800/54
400 01 Ústí nad Labem
www.icuk.cz

New financial instruments to support development of enterprises in Usti Region

A Policy Learning Platform Peer Review

14th-15th November 2023

Final Report

1. Brief presentation of the beneficiary and its motivation to host a peer review

This Peer Review was hosted by Innovation Center Úsí nad Labem (ICUK).

Since 2015, when the Innovation Centre of the Ústí Region was founded by the Ústí Region Office, Jan Evangelista Purkyně University and the Regional Chamber of Commerce, we have been one of the carriers of the vision of a functional Innovation ecdosystem in the region and a persistent fighter for its creation.

We are a respected teammate in the transformation of the Ústí Region into **a place where citizens, students and entrepreneurs will like to stay**, where they will return and where talented people with the desire to participate in this change will also actively come.

We are a **responsible partner** to our founders in the **preparation and implementation of strategic priorities** for the **development of entrepreneurship** and the **knowledge economy**. With insight and an open mind, we take inspiration from the best at home and abroad, share our ideas and experience with other partners in the region and together with them create and implement new solutions that support entrepreneurship, business and cooperation of active people in our region.

We **help local companies to launch their entrepreneurial dream** and grow beyond our region's borders, connecting partners from the world of business, research and education, and strengthening our region's attractiveness to high value-added investors. Helping companies grow. We are **building the innovation ecosystem of the Ústí Region** and we are striving for its development through independent projects that will bring new economic opportunities, better conditions or new tools and services for the inhabitants of the region.

In May 2023 **ICUK was successfully certificated by European Business Network** and is now full member of this European organisation.

The Ústí Region is strongly affected by structural changes in the economy. In the course of the economic transformation from a planned market economy, there was a gradual decline in traditional industries (including mining, textile, food, chemical and metallurgical industries) and changes in the structure of the regional economy.

Even so, **some traditional industries have retained their significant importance** for regional macroeconomic indicators and employment, however, due to the unfinished transformation, it is possible to expect a further decline in previously important industries (especially brown coal) with negative consequences for the economy and the labour market in the region.

Without energy and mining, along with a whole range of interacting factors, the possibility of other applications affecting the economic situation, it is also necessary to mention, these sectors have also been the subject of many innovations in the long term and contributed to the results of research and other activities in practice.

And it is precisely this unique and, at the same time, specific know-how that needs to be used towards the overall transformation of not only the energy sector, but also the economy of the region as a whole. This regional know-how can be a unique opportunity for the future of the region. The main goal of the so-called Green Deal for Europe is to achieve a climate-neutral circular economy.

However, not all states and regions have the same starting position, and especially those whose national economy is built on resources such as coal will need far greater investments than others. That is why the Just Transition Mechanism was create to ensure fair access to all states and disadvantaged ones to help achieve these goals.

The transformation strategy of the Ústí Region, which was (together with 2 other regions of the Czech Republic) identified as the region most threatened by the transformation process to a climate-neutral economy and facing serious socio-economic problems, **is based on 4 main pillars**:

1.) Diversify the regional economy through the creation of new opportunities in developing fields and the stabilization of the region's key industries and their adaptation to the conditions of a climate-neutral economy. All this with an emphasis on maintaining employment and creating new job opportunities.

2.) Increase the qualification and retraining of workers affected by climate change, including professional training. Help current and future workers adapt to new job opportunities. Pay special attention to vulnerable groups that are disproportionately affected by the adverse effects of the transformation.

3.) Ensure enough affordable clean energy, use resources efficiently and reduce dependence on fossil fuels.

4.) Use the area after coal mining and related industrial activities have ended for new activities in order to revitalize these locations.

2. <u>Specification of the policy challenge encountered</u>

The **Ústí Region** is going through an **economic transformation**, the **decline of coal mining** and **the decarbonization of energy-intensive industry**. **To deal with the impacts, the Fair Transformation Fund (FST) is used**, which makes it possible to use not only grants but also other instruments of financial support for SMEs to support the diversification of the economy. In the Czech Republic, there is still rather less experience with the use of financial instruments, in a combination of public and private funds.

There are venture funds and programs of the National Development Bank co-financed by the EIB, but the country still has little experience with matching such instruments with the use of the ERDF and the Just Transition Funds at the regional level. The Fair Transformation Fund (FST) is intended for three coal regions of the Czech Republic. The regions prepared so-called transformation plans containing their priorities, including business support.

From this, the Ministry of Environment, as the managing body, prepared one operational program for all three regions. Partial calls of the program are then prepared for individual regions in close consultation with their experts. The region is a member of the monitoring committee, which is the main governing body of the program. ICUK, the Innovation Centre is the so-called implementation unit of the smart specialization strategy (S3).

From this position, it prepares policy proposals for the support of business for the region, prepared the above-mentioned transformation plan and, for example, it designs innovative and digital vouchers financed from the JTF. ICUK also participates in the negotiation of measures with the program's governing body.

ICUK processes documents for the monitoring committee of the Ústí region, meeting is regularly every month and they prepare regional policies. Every quarter there is a meeting of the monitoring board - representatives of the region + ICUK.

In addition, the Region is a recipient of the Smart accelerator, thanks to which policies are created. ICUK is the expert guarantor of the project.

The first programs are launched in the region together with the National Development Bank allocation of EUR 25Million, but they are more suitable for traditional companies with a good rating and do not solve the market failure to which a number of companies are exposed – in particular at their starting phase.

As part of the preparation of the loan program, we had preliminary processed a scoring system for six highly innovative companies. Unfortunately, the program is set up in such a way that only one out of six passed the credit evaluation. We asked the monitoring committee for an evaluation after six months and we would then like to propose changes to the program.

We aim at looking for ways to make successful use of the Just Transition Fund by promoting the development of financial instruments that genuinely match the needs of the Czech innovation ecosystem, for instance: Proof of concept fund /acceleration fund/ - intended for projects in the stadium idea, startups, academic and corporate spin-offs; Seed fund – designed for established startups with an MVP (minimum viable product);

Mezzanine/Threshold fund – intended for existing companies with growth potential /larger startups, medium growth companies, or midcaps/.

Regional policy challenges is utilization of transformation – loans . Interest-free transformation loans are dedicated to support the investment activities of small and medium-sized entrepreneurs active in three just transition regions, i.e. Moravian-Silesian, Ústí nad Labem and Karlovy Vary regions.

The National Development Bank (NRB) and the Ministry of the Environment (MŽP) have prepared a program of interest-free loans to support the investment activities of small and medium-sized entrepreneurs in selected regions of the Czech Republic. Entrepreneurs in coal regions, i.e. The Moravian-Silesian, Ústí and Karlovy Vary.

Brand new activity is agreement with other seven regions, or better said their innovation center, about creating new entity, innovation seed fund which could be a vehicle for co-founding from Ministry of Industry and Trade Czech Republic and as well Just transition mechanism program. Important is now presentation this initiative to local politicians and designing fund for local challenges.

Questions to be answered by the peers:

A) Policy level

- What type of financial tools could you recommended for SME in transitive regions.
- How to present it to political representants. (Comparison grants x financial tools)
- What are the financial tools best practice in smaller EU countries and/or in transitive regions.

B) Fund design

- Estimation number of investment deals per year
- Estimation about volume dedicated to whole regional fund in seven regions (minimum fund budget for successful risk sharing portfolio)
- Estimation how many funds could be invest in region like we are in five years.
- Fund conditions for SME
- How to deal with fund profitability (success rate, reinvestment).

C) Fund management

- Possible risks and how to manage them.
- How to manage (and present) investment failures
- How to manage fund, involvement of politicians?
- How to manage public aid.

3. <u>Participants</u>

List of Participants
Innovation Center of Ústí nad Labem ICUK • Zdeněk Hušek, RIS3 Manager • Kamila Kmentová, Education Manager • Lucie Podrápská, Strategy Manager
Peers • Juan Carlos Martinez Barrio, CEEI-Burgos, Spain, Director of Projects Development Programme and Project Manager • Dr Csaba Novák, IFKA, Budapest, Hungary, Head Of International Programmes • Daniel Zimmermann, LMF asbl, Germany, Director and co-founder • Mirosław Miller, Wroclaw University of Environmental and Life Sciences, Poland, Professor - Coordinator of R&D Programmes
Regional Stakeholders • Councillor Iva Dvořáková - area of entrepreneurship, innovation and transformation • Councillor Růžička Jan – financial area • Jana Nedrdová - Department of transformation of the region • Iva Tomešová - Business Support, Innovation and Transformation Department • Václav Papřok member of Department of Financial Management and Control • Renata Černá – Department of projects and funds
Interreg Europe Programme • Ilaria Ramaglioni, Policy Officer

Interreg Europe Policy Learning Platform • Elena Ferrario, PLP Thematic Manager • Luc Schmerber Thematic Expert, SME Competitiveness • Rene Tonnisson, Thematic Expert, SME Competitiveness

4. <u>Policy Recommendations</u>

1. What type of financial tools could you recommend to best support SME in transition regions like Usti Region?

a) <u>Generic recommendations</u>

It is strategic issue whether to target:

- the new, greener and innovative activities of traditional industries and/or
- to target completely new, greenfield activities to replace old activities.

Experiences from Hungary show that:

- Innovative activities of mature companies are needed on the short-term to absorb the funds available and bring transition forward
- Startups have comparatively little fund absorption capacities on the short-term but are needed to develop industrial relevance in the future
- Repayable instruments should be foreseen, especially for investments in infrastructure, technology lines, technology purchase, etc.
- Always link funding to training/coaching/mentoring activities (smart money)
- Focus on what is not covered by the market

In the case of the use of **Just Transition** mechanism:

- The **time available is short** and setting up new investment instruments might take too much time to be able to spend the money before closing of the programme
- Consider **using/adapting existing instruments to the needs of the industrial transition**

The **case of grants**:

- **Repayable instrument should be prioritised over grants**

- Grant instruments (if any) should be linked to the beneficiary's **own contribution**, depending on the risk associated with the instrument
- Grants are generally popular and can be used to **generate a funnel of projects** to be then moved to an ‚investment fund‘, acting on the basis of repayable instruments (loans, equity schemes, ...)

b) Practical recommendations

Knowing the needs and absorption capacity of clients is crucial

- FI should be **well targeted**.
- In the planning phase a thorough and **personal knowledge of the potential clients** in the region and their **specific needs** and business considerations can be a huge advantage. An overoptimistic planning is a major risk for new financial instruments.
- The programme implementation people should personally know the company players and their attitude towards transition (greener, ...). **Attitude is very important**.
- **Focusing on numbers might lead to overestimate** the potential of new funds. The use of aggregated statistical estimation of the size of the potential target for the fund does not lead to a good estimate.
- Experience from Hungary show **in regions under restructuring, the firms are much more willing to try new business models**, industries and are open to new ideas and technologies. The most dynamic IT or bio clusters in Hungary are in these regions.
- **Critical mass** is thereby a key factor. Some support actions might be better treated on the national level (example: funds dedicated to the creative and cultural industries) whether others are well suited / can be better treated on the regional level (example: green tech).
- **Local business support organisations and development agencies** can help identifying the most suitable businesses and evaluate the potential use of the instruments.

c) Practical recommendations

Generating trust and acceptance of new schemes

- **Bottom-up processes** are useful for involving local communities in the design of the economic transition and **generating projects.**
    - **Living Labs** methodology
    - Bottom-Up Business Opportunities concept
- **Showcasing successful transition practices** can have a strong impact on SMEs' behaviour

Examples from Hungary showed that visiting 'high-tech' working real production units can significantly increase the readiness to change of SMEs. See here for more information on the related practices.

- The funding offer needs to be **attractive** and include a **strong protection of the SMEs** (IPR, independency from funding organisation) to **generate trust** in the scheme.

d) Practical recommendations

Piloting can help validate concepts and avoid large failure

- **Running pilots through calls for proposals enables to check the feasibility of new support instruments:**
  - Step 1 – pilot
  - Step 2 - upscale
- **Suggestion: Initial budget smaller for the first call/year, to be increased if proved worth it. Can be a way to move faster as developing new tools might take a long time**
- While the piloting approach is to be recommended in general, **in the case of the Just Transition mechanism, the time available might be too short** to have such a piloting phase and then create a new instrument.
- *Example: the microfinance fund from Burgos has been designed and piloted in the framework of transnational collaboration projects, such as e.f the Interreg Europe project ATM for SMEs.*

e) Practical recommendations

Follow a project-based approach rather than a financial-instrument based approach

This approach suggest to first **create a comprehensive approach to industrial transition in the region –** key aspects are:

- **Projects** bringing the transition forward
- **Human capital** (persons, skills) needed to implement the projects
- **Collaboration** (because we work across sectors and disciplines) generating relevant and promising projects

All 3 aspects should be treated simultaneously.

- **Projects come first – financial tools second**
- Identify **specific needs** in terms of infrastructure / collaboration and human capital / skills for the realisation of a given project.
- Then identify **suitable tools** to fill the need
- Likely a **combination of different existing, improved or new financial tools** will be needed to support interesting projects
- **Create places where collaboration can happen** – do not create only a fund – create an attractive place for smart people. Those people will generate projects. This can be for instance a new technology facility.

f) <u>Practical recommendations</u>

Follow a project-based approach rather than a financial-instrument based approach

The project-based approach implies a flexible use of different funding schemes, according to the needs of each project.

Examples of potential schemes are:

- **Apprenticeship fund:** grant for the employment of a university graduate (e.g. average salary in the sector for 12 months)
- **Reskilling fund for workers** in traditional sectors who want to retrain or start their own business.
- **Fund for the organisation and launch of a Living Lab** in the area of green technologies
- **Loan facility for the public sector:** energy and transport infrastructure, district heating, energy efficiency measures (including building renovation) and social infrastructure.
- **Equity Investments:** Encourage the creation of a regional venture capital fund, which can take equity stakes in start-ups and SMEs.
- **Guarantee Instruments:** Develop guarantee schemes to reduce the risk for private investors and banks when they finance SMEs
- **Convertible Loans:** Offer convertible loans that can be turned into equity if the SME reaches certain milestones, which can be particularly attractive for start-ups in the AR, VR, and AI spaces
- **Innovation Vouchers:** Introduce vouchers that SMEs can use to purchase consultancy, R&D services, or access to high-tech infrastructures.
- **Voucher for the start of research into a new technology:** subsidy for the implementation of commissioned R&D work by the entrepreneur to a selected laboratory, research centre, university, etc. Voucher value up to EUR 200,000, own contribution 30%.
- **FI for the establishment of a new startup company:** Voucher value up to EUR 200,000, own contribution in the form of a private investment in this company of at least 30% of the grant.
- **FI for the professional activation of women**
- **FI for the organisation of a social enterprises** (cooperative, „silver economy", disabled, pensioners)
- **Repayable instrument for investment** in a production line, marketing, export, mentoring, preparation of a project application

g) <u>Practical recommendations</u>

Involvement of University – knowledge organisations is crucial

- Need to **build strong relationships between businesses and the local research community**

- **Universities should** be seen as
    - Providers of human resources
    - Experts – providers of knowledge and technical skills
    - Drivers for innovation projects
        - Innovation nest rather than individual invention – e.g. prepare laboratories for the future technical developments => flexibility of funding is important
        - Invest in a combination of infrastructure + people
        - Create the feeling of something new
- Examples from Poland
    - Wrocław Research Centre EIT+ (ERDF)
    - EIT+ Hybrid Companies Accelerator (ERDF)

h) <u>Specific examples of financial tools</u>

Example 1: Setting up a microfinance fund – The example from Burgos

DEFINITION

- **Microfinance** covers funding / investments **lower than 25.000 EUR**

BENEFITS OF MICROFINANCE FUNDS

- Quite suitable for **maintain smaller businesses in the region** – young entrepreneurs, e.g. in depopulated areas
- Micro investments can generate an **initial momentum for further larger innovative / transformative activities**
- **Repaid funds can be used for further investments,** contrary to vouchers
- Small initial amounts (~ 2 Mio. EUR in Burgos) are enough to setup funds
- It is possible to setup **different local funds** within one same larger region
    - Local funds can answer local needs
    - Competition among funds stimulates quality

RECOMMENDATIONS FROM THE BURGOS CASE

- Microfinance funds should have a **broad understanding of innovation: technical, technological, commercial…**
    - Special focus on commercial aspects as one of the most powerful drivers of Innovation.
    - Close-to-market approach, product development and business modelling as essential components of Innovation processes.
    - Traditional sectors are also concerned with innovation – **do not discriminate any sector**

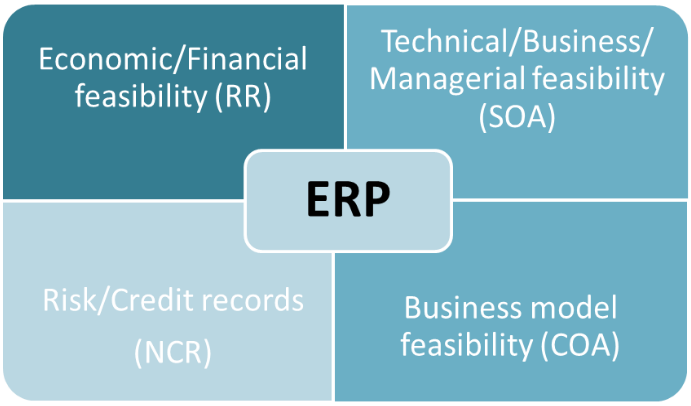
- A sectoral approach is not recommended on the local level – **generating enough investment (critical deal flow mass) is to be prioritized**
  ➔ There is a need to **involve local agents** (economic development agency, incubators, …) **to identify investment opportunities**. It is necessary to act proactively as an investor, not passively like a distributor of grants.
- Target as possible an **area not covered by the market**. In Burgos, it was possible to invest without requiring guarantees or collaterals from the entrepreneurs, which differentiates the scheme clearly from traditional models from banks.

EXAMPLE OF A PRACTICAL IMPLEMENTATION - CEEI-BURGOS MICROFINANCE FACILITY
Micro credits

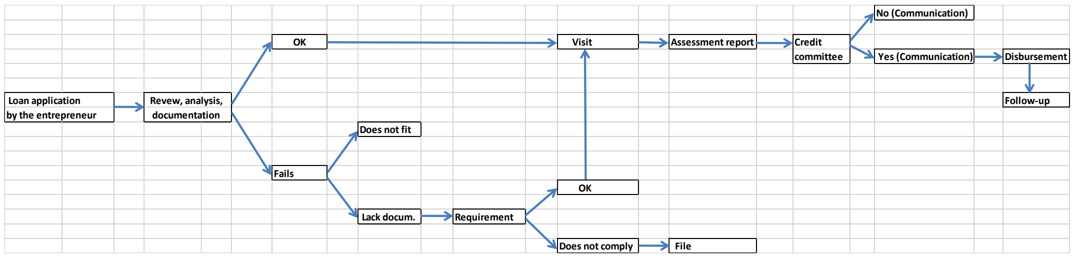
- No guarantees/No collaterals
- 4/5 years
- 6 months grace period (Optional)
- 3-1,5% of interest rate
- No fees
- Maximum 25000 €
- Funded by the Provincial Government of Burgos /SODEBUR
- Target group: Entrepreneurs and SMEs from Burgos Rural Areas
- Administrative management: SODEBUR
- Operative management and risk assessment: CEEI-Burgos

Risk assessment methodology based on:

- ESTIMATED RECOVERY PROBABILITY (ERP)
- RISK RATIO (RR)
- STRUCTURAL OPERATIONAL ANALYSIS (SOA)
- CREDIT OFFICER ASSESSMENT (COA)
- NEGATIVE CREDIT RECORD (NCR)



How it works



<u>Specific recommendation 1– setting up a microfinance fund</u>

RESOURCES FROM INTERREG EUROPE

- Good practices from the ATM for SMEs project – click here

Example 2: **Specific examples of financial tools**

- Investment fund with support of the EIF – InvestEU programme
- Wallimage case (Belgium)

<u>Investment fund with a long-term perspective (equity/guarantee)</u>

- When thinking about new funds, consider the opportunity to get support from the EIF/EIB through the InvestEU programme:
  - Fund design
  - Due diligence
- Support areas:
  - Portfolio Guarantee Products
  - Capacity Building Investment Product
  - Equity Fund

InvestEU Fund

A. Portfolio Guarantee Products

SME Competitiveness	Sustainability	Innovation & Digitalisation
Cultural & Creative Sectors	Microfinance & Social	Skills & Education

Cultural & Creative Sectors

This sector for over 4% of GDP, 10% share in total companies in services and also provide for approximately 7 million jobs.

Despite their important role, CCS companies face difficulties to access finance, mainly due to the perceived complexity of their business models, associated risks and intangible nature of their assets.

The Cultural and Creative Sectors Portfolio Guarantee Product aims to therefore enhance access to finance to SMEs and other eligible enterprises operating in the CCS, therefore supporting this creative ecosystem, consolidating its resilience and allowing it to adapt to the challenges ahead.

A Case study: Wallimage

The EIF's CCS Guarantee was provided to Wallimage for

- **SME Loan Support**
- **Focus on equity investments for strategic capital consolidation and profitable exits**.
- **Loan maturity**: 5-7 years, extendable to 10 years in special cases
- **Collateral**: Assets used for the business activity

2. Development Loans for Production Projects

- Covers all development phase elements: writing, casting, legal, scouting, etc.
- Loans are reimbursed if the project enters production; not reimbursed if not realized.
- Goal: Enhance commercial quality of audiovisual projects in Wallonia
- Maturity: 2-4 years
- Collateral: IP rights

3. Video Game Industry Support

- Financing model similar to audiovisual sector, tailored to gaming industry needs.
- A. Video Games Debt Financing
- B. Start-up gaming studio
- Aims to assist start-up gaming studios with the help of CCS Guarantee.

1. **Guarantee structure:**

Maximum Portfolio Volume	EUR 16,000,000
Guarantee Rate	70%
Maximum Guarantee Amount	EUR 11,200,000
Guarantee Cap Rate	25%
Maximum Guarantee Cap Amount	EUR 2,800,000
Availability Period	3 years

2. **Eligible debt financing**:

Type of underlying transactions	Participating loans, convertible loans and senior loans
Indicative contractual terms	Standard CCS contractual terms will apply.

B. Capacity Building Investment Product

The InvestEU Capacity Building Investment Product aims to support the EU's emerging microfinance & social entrepreneurship and skills & education ecosystems.

The purpose of the EIF's Capacity Building Investment (CBI) Product is to build up the institutional capacity of Financial Intermediaries that have not yet reached sustainability (including Greenfield Financial Intermediaries) or that are in need of risk capital to sustain their growth and development in the microfinance, social entrepreneurship or the skills and education space.

The Target Areas

- Microfinance
- Social Entrepreneurship
- Skills, education and Training

Eligible Financial Intermediaries

Banks	Guarantee institutions	Microfinance institutions
Crowd-financing platforms	Non-bank financial institutions	Loan and/or investment funds
Credit Unions	Education & training providers	& more

C. Equity Fund

Thematic Strategies

The scope of InvestEU Equity covers several specific sectors of activity, grouped into Thematic Strategies.

A financial intermediary applying to InvestEU Equity will therefore be expected to address in their investment strategy one or more of the following Thematic Strategies. Under each one of these there also exist a set of underlying Target Areas.

Click on each area to discover them in more depth.

Capital Markets Union (including debt funds)	Enabling Sectors	Climate & Environmental Solutions	Digital & Cultural and Creative Sectors	Social Impact

2. <u>Benefits from the perspective of political representatives</u>

Leveraging private investments: Public revolving funds able to leverage further bigger private investments. Build on good practices and experiences in Usti:

- Benchmarking of instruments operating in similar Central European regions
- Use case studies from other EU regions that have successfully implemented similar financial tools, emphasizing the long-term economic growth and job creation that resulted from such investments. (Hungary, Poland)

- Analysis of financial instruments used in previous periods in the region with proposals for adaptation to the current market situation: energy crisis, climate crisis, Green Deal, etc.

Linkage to strategy implementation: Indicate how the new instruments will accelerate the implementation of the RIS strategy for Usti

Fighting depopulation: Instruments with impact on how to slow down and reverse depopulation processes in less developed regions

Sustain: ability, long-term impact: Compare the long-term sustainability and growth potential of investing in intellectual property and high-impact industries versus traditional grants.

3. **<u>Setting up a regional investment fund</u>**

1. What would be optimal size of the fund and minimum fund size?

- Need for a **market study** or similar. Aggregated regional numbers are of little use here. The attitude and willingness of the individual companies to change in exchange for cleaner technologies should be known in advance. (see knowing the market)
- Determine the minimum fund budget required for a diversified and risk-mitigated portfolio, **possibly starting with a pilot fund size** based on the number of potential deals identified.
- Setting up new risk capital funds **can be extremely time consuming it could be as long as two or three years**
- An alternative is to consider the possible **adaptation of existing instruments** to new funding requirements.
- In practice:
    - Microfinance funds can be small (2 Mio. EUR in Burgos)
    - Investment funds need a **minimal size of 15-20 Mio**. EUR considering the setup and management costs

2.What would be the optimum number of funds in Usti region during next five years?

- 1 (one) or 2 (two) funds might be considered, as potential project numbers do not necessarily justify a sophisticated structure and division of labour between funds

    one regional fund for mature investment targets and another one for start-up and spin-offs in the region. It should be a question of strategy. In Hungary most funds turned towards mature companies as adsorption pressure became high.

    Potential risk capital investments transactions with green targeting can be very difficult to find. And so, special funds may not be justified due to modest numbers that are ready to become an investment target.

    Investment period should be long: minimum 7 years. Rather 10 years in total.

- Based on its performance and the evolving needs of the region, consider adding one or two more funds over the next five years, focusing on different stages of business development (e.g., seed, growth).
- The difficult bit is how these relatively small amount can really contribute to replacing and greening large operations like coal mining and coal-based energy generation. In order to have significant impact of carbon emission of coal use small risk capital-based proposals should be combined with larger credit-based funds.
- The role of a Seed Fund should be better pursued with micro grants instead of capital, and the results of the seed activity should be channeled to JUST capital investment proposals

4. **What would be the main investment criteria for making investments into regional SMEs?**

- Innovation Potential: Focus on SMEs with high innovation potential in AR, VR, and AI within the cultural and content industries.
- Sustainability: Ensure alignment with the Triple Transition goals, emphasizing economic viability, social impact, and environmental sustainability.
- Scalability: Preference for businesses with potential for regional and international scalability.
- Management Team: Evaluate the strength and experience of the SME's management team.
- Contribution to decarbonizing the economy

5. **What would be the optimal number of investment deals per year in Usti region?**

- Realistic Target: Aiming for 3-5 investment deals in the first year, scaling up as the fund matures and gains more insights into the regional market
- Depending on the demand and size of the funds the number of investment deals could be increased.

6. **What should be the expected profitability (success rate, reinvestment) of the fund?**

GENERIC REMARKS

- Focus on a professional feasibility and risk analysis rather than in guarantees and collaterals when assessing operations (Excellent political impact and marketing tool) – every project should have the same chance of success

- Establish a reinvestment strategy for returns generated from successful investments. Profits should be reinvested into the fund to support additional SMEs and foster a sustainable investment ecosystem
- Set realistic success rate targets based on industry benchmarks

  SUCCESS RATE
- **Success rate**: at least 60% of investments will bring positive returns to the fund after the end of the fund de-investment period of minimum 7 years or maybe 10 years (lower failure rate with mature companies)
- **Success Rate**: Aiming for a internal rate of return (IRR) of around 10-15% qnd Return of Investment (ROI) 2-3 times in line with venture capital norms, understanding that high-risk ventures often have lower success rates.

7. What are the main investments risks and how to manage them?

- Business cycle, unexpected structural breaks in the market, input cost shocks, regulatory shocks
- Market Risk: Diversify investments across different sectors and stages of business development.
- Liquidity Risk: Ensure some investments are in more liquid assets to manage cash flow needs
- Operational Risk: Employ experienced fund managers and advisors..
- Transparency: Be transparent about failures, sharing lessons learned.
- Portfolio Approach: Spread risk across a portfolio of investments to mitigate the impact of individual failures.
- Financial risk assessment as a must focused on the project itself and the promoter (Entrepreneur, SME, Start-up…)

8. How to manage (and present) investment failures?

- Create a transparent process for dealing with investment failures, ensuring learning and adaptation for future investments.
- A precalculated failure rate should be set up and should be a basis of the business plan of the management company based on the local knowledge of investment targets. The concept of calculated risk should be embraced

- To be presented as a default ratio as in the financial markets (e.g.: NPL30) always highlighting that it is always better than a grant which is never recovered from the Administration point of view. Managed by follow-up and recovery actions.

9. **How to manage fund, and should there be any involvement of politicians?**

INVESTMENT BOARD

- The investment board should be made up of regional and industry experts
- Politicians or their representatives should be **observers on boards** without voting rights. Advisory boards could be used also.
- **Inclusion of administration and stakeholders in the decision process** (Credit committees of microfinance funds…) and involvement in the marketing and communication actions.
- Politicians tend to soften up conditions so that the reach of the programme goes far beyond the original scop. Therefore, one should **set important conditions in stone in documents where it is difficult to soften up** (OP document, international contract)

MANAGEMENT

- The fund should be **managed by professionals** with expertise in venture capital, innovation, and regional development.
- Political involvement should be limited to oversight and ensuring alignment with regional development goals.
- Establishment of a **dedicated management institution**, preferably a company, which has specific transformation targets and indicators to achieve

TECHNICAL MANAGEMENT

- **One administrative procedure for all elements of the products and one agency/fund manager / Create one shop stop (we needed a full EU budget period to learn that)**
    - **Avoid parallel business processes** for the grant and for the loan giving as lead times can become unbearably long.
    - Avoid using **separate IT systems**, for example one for loans and one for grants. Avoid parallel processes at all costs. Blame game emanates.

9. **How to manage state aid related aspects?**

- **Ensure compliance with EU state aid rules**. This involves setting clear guidelines on how the funds are allocated to prevent market distortion and ensuring that the aid is proportionate and targeted.
- If there is grant part regional SME aid intensities apply. Ensure that the voucher scheme and other financial tools comply with EU state aid rules and regulations.

5. <u>Possible calendar of implementation</u>

Calender of implementation of the proposed recommendationis added to this document as an attachement.

6. <u>Conclusions</u>

Following the peer review, regional committee for competitiveness (tripe helix consultation board for regional innovation ecosystem) recommended to prepare selected financial tools especially for funding from EC JTF/JTM. Ústí S3 team will be responsible for consultation process, especially with Czech JTF managing authority, National development bank and for creating necessary documents. There will be also prepare preliminary law analysis with definition of potential pathways as well as evaluation of potential risks.

There are two running actions, soft loan scheme and cooperation model with local University. This actions could start immediately, other activities will start after approving from regional councillors (see gantt scheme).There is also ambition to prepare or to join consortia for Interreg Europe project focus on detail set up microcredits and/or equity scheme for start ups and University spin offs.

Ústí nad Labem, 18th December