



Access to finance for innovative SMEs

A policy brief from the Policy Learning Platform
on SME competitiveness

July 2017





Entrepreneurship is a powerful driver of economic growth and job creation in Europe: it creates new companies and jobs, opens up new markets, and nurtures new skills and capabilities. But there are many barriers in Europe which explain the fact that less than 40% of Europeans consider self-employment as their first choice. By contrast in the USA and China this proportion is much higher (more than 50%).

The Entrepreneurship 2020 Action Plan (https://ec.europa.eu/growth/smes/promoting-entrepreneurship/action-plan_fr) of the EU Community highlight the tough environment for entrepreneurs in Europe: education does not offer the right foundation for an entrepreneurial career, difficulty in transferring businesses, the fear of punitive sanctions in case of failure and of course the difficult access to finance.

Access to finance is one of the levers for growth for SMEs: without adequate funding and without liquidity, no business can operate, invest and grow. SMEs have historically relied on bank lending and consequently the current bank credit constraints due to economic crisis for the last 10 years have a disproportionate impact on SMEs. The specific problem of the access to finance constraints the development of SMEs in Europe and is objectively a major issue. The reluctance of commercial banks to finance SMEs obliges to become creative.

In fact, the topic is very broad, because the financing needs are very dependent on the nature of the companies (size, business sector, technology's maturity, loan rates...) and also on the different phases of the SMEs life-cycle: this is particularly true for innovative R & D companies seeking funding in order to design a pre-industrial prototype for instance but also generally for the innovative SMEs in the early stage of their business. Moreover, the methods of financing have changed substantially in recent years: in addition to traditional financing tools (equity, convertible loans, commercial loans, public soft loan...), new forms of financing have been developed for the last 10 years, such as the use of crowdfunding or business angels. That makes things difficult for the entrepreneurs.

This Policy Brief is devoted to the specific problem of the access to finance for innovative SMEs in Europe. After referring to the recommendations of the European Commission on this issue and presenting the basics of the COSME program, which makes changes, past or current European projects dealing with this issue, directly or indirectly, are being developed.

1. The problem of the access to finance for innovative SMEs in Europe

Entrepreneurs particularly have difficulties raising finance in the early stages of their innovation process. That's the reason why the issue of the access to finance for SMEs is highlighted in the "Entrepreneurship 2020 action plan" of the EU Commission (2013) : "More must be done at both European and national levels to overcome market deficiencies, including exploring alternatives to bank lending for SMEs, to complement the limited private financing available and to make information on funding more easily available" (https://ec.europa.eu/growth/smes/promoting-entrepreneurship/action-plan_fr).

"It is also important to increase the quality and financial returns of start-up projects. Financial support for testing, demonstrating and piloting new technologies, strengthening venture capital, angel investments, incubators and loans for high potential SMEs are some of the



areas where action is possible. Entrepreneurs need funds to commercialize research and development and test innovative business models”

(https://ec.europa.eu/growth/smes/promoting-entrepreneurship/action-plan_fr).

In this context, much has changed over the past few years. Indeed, support for these areas is proposed by the European Commission under the COSME Programme and Horizon 2020, and are reinforced under the European Structural Funds.

An important component of a successful entrepreneurial ecosystem consist of an array of early stage investors (venture capitals and business angels) that provide seed and first round equity investments. These investors use an extensive network of peers and provide valuable knowledge and support about the market and the development of the venture "smart money". These investments may also be spurred by fiscal incentives.

It also should be remembered that in 2008 the Commission created the Enterprise Europe Network, a partnership with over 600 hosting organizations, one of whose tasks is to provide businesses and would-be entrepreneurs with the necessary information on access to EU funding and EU finance. To date, better information on EU support is still a major business request. The Commission is working, together with stakeholders, to strengthen the Network to make it more active and effective.

2. The Programme for the Competitiveness of Enterprises and SMEs “COSME”

The Programme for the Competitiveness of Enterprises and Small and Medium-sized Enterprises (SMEs) - COSME - is the Union’s programme to strengthen the competitiveness and sustainability of enterprises, to encourage an entrepreneurial culture and to promote the creation and growth of SMEs.

COSME has a budget of over EUR 1.3 billion to fund these financial instruments that facilitate access to loans and equity finance for SMEs where market gaps have been identified.

Thanks to this budget, it will be possible to mobilize up to EUR 25 billion in financing from financial intermediaries via leverage effects. The financial instruments are managed by the European Investment Fund (EIF) in cooperation with financial intermediaries in EU countries.

COSME contributes to the overall objectives of the Europe 2020 strategy on smart, sustainable and inclusive growth while seeking to optimize synergies with other EU programmes such as Horizon 2020 and the European Structural and Investment Funds (ESIF). As set out in the COSME legal base, these objectives are:

- improving access to finance for SMEs in the form of equity and debt;
- improving access to markets, particularly inside the EU but also at a global level;
- improving framework conditions for the competitiveness and sustainability of enterprises, particularly SMEs, including in the tourism sector;
- promoting entrepreneurship and entrepreneurial culture.

Regarding the first specific objective “Improving access to finance for SMEs”, the COSME Regulation specifies that at least 60% of the total budget has to be allocated to the financial instruments for 2014-2020.

In practical terms, a loan guarantee facility (LGF) is implemented. These guarantees for debt financing (including via subordinated and participating loans, leasing or bank guarantees) which shall reduce the particular difficulties that viable SMEs face in accessing finance either due to their perceived high risk or their lack of sufficient available collateral.



Moreover, through the EFG risk capital funds (Equity facility for growth) can be supported which invest into SMEs at the growth stage, predominantly on a cross-border basis, or which help portfolio companies to grow beyond their national markets with a view to supporting the development of a self-sustainable pan-European risk capital market.

3. Good practices from European regions

4 projects of the Interreg Europe IVC program have been identified in connection with the problem of access to financing for innovative companies.

[Interreg IVC DIFASS](#) was a 3 years project aiming to unlock potential for innovation, internationalisation and sustainable growth of SMEs in Europe by improving access to finance. **Innovative SMEs are often faced with problems when obtaining loans from commercial banks and intermediaries as valuing risks in technology innovation** or foreign markets is problematical and as SMEs often cannot provide sufficient collateral. Resulting from the global financial crisis, requirements to obtain a loan have even been further increased. Thus, it becomes a field for stronger engagement of the public sector, but public financial resources are limited and need to be used as effective as possible. The Development of Interregional Financial Assistance to SMEs and of non-grant instruments (DIFASS) is therefore an important task. The partners have teamed up to exchange experiences on good practice established in 20 European regions, to develop or improve policies in that field and to support the transnational transfer of selected good practices towards more regions. Moreover they were supported by scientific partners: they elaborated a work plan for their analysis of the background mechanisms of good practice, and a template for the collection of detailed information about the already identified good practices, that has to be filled in by the partners.

[Interreg IVC MINI EUROPE](#) was a 3 years project aiming to exchange and develop regional policies in SME development, focussing on the main theme of providing a transparent infrastructure for innovation to SMEs. The main goal was to improve existing instruments and import new instruments in order **to strengthen regional infrastructures to support SMEs in innovation**. The partnership combined the experience of 8 regions from all parts of Europe. By bringing together and capitalising their methods and experiences, all partners could strongly improve their performance to strengthen regional SME development. This has resulted in a match between importing and exporting regions. In this context, Valencia (ES) started importing the Financial Engineering programme from Veneto (IT), which combines a guarantee system for innovative investments, a revolving fund for SME's innovative investments and a venture capital and private equity fund. The financial engineering programme leads to better access to finance and reduced costs for innovation.

[Interreg IVC NEEBOR](#) (Networking for Enterprises in the Eastern External Border Regions) was a 3 years project grown out from a wide European initiative aiming at the collaboration of regions from 8 European countries on the external borders of the European Union. Core elements of successful SME development and innovation policies in these areas are cross border business cooperation with non European neighbouring countries, and **better structures of access to knowledge and access to finance for SMEs in peripheric areas**. The specific objectives of NEEBOR was to develop a clear understanding of the external border regions (key challenges, key strategies, key actors and key actions on SME development and innovation) and to exchange good practices which can help to unlock business potential in these regions as cross border business cooperation, access to finance and access to knowledge for SMEs.



The main goal of [FIN-EN](#) (Sharing Methodologies on Financial Engineering for Enterprises) was to set up a wide and stable network between regional and national authorities across Europe where to discuss each phase of financial engineering operations' implementation and the underlying financial instruments in order to find concrete solutions to similar problems. The partners worked on the programming, implementing and evaluation phases of financial engineering operations, to deliver a Financial Engineering Handbook, including the traps to avoid, best practices to adopt and the differences from one country to another, a methodology facilitating the dissemination of Financial Engineering Instruments.

The current Interreg Europe programme also provides support to partners which intend to work together to address the challenges of the access to finance for SMEs and particularly for innovative SMEs seeking funding in the early stages of their businesses. Three projects on this theme which have recently been approved are highlighted below.

[SPEED UP](#): this project launched on April 2016 is mainly focused on business incubation but also on access to finance, although marginally. The overall objective of the project is to trigger policy change in the partners regions improving the implementation of the policy instruments under Structural Funds programmes dedicated to support of entrepreneurship, in particular concerning **business incubation**. The policy instruments tackled by the project are the ERDF Operational Programmes at regional or national level enabling the creation of new companies through business incubators. Policy change in the partners regions will occur through a collective multidimensional and dynamic learning process at policy level and involve, along to the partner organizations, relevant stakeholders of the concerned policy subsystems. The access to finance is just one of the topics, linked to financial sustainability, analysed during the SPEED UP project: improve the services provided by the business incubators and ensure their financial sustainability.

In the frame of the project a conference was held on January 2017 in the city of Florence. Speakers highlighted that SMEs face difficulties to structure projects and to participate in funding calls because of the rigidity of the calls, the lack of communication towards SMEs and the deficiencies in the public structure and in internal competences of public administrations. **The early stage financing in business development of innovative technologies for SMEs and the role of the bank in the management of co-financed loan funds for SMEs is also a problem.**

Regarding the specific topic of early stage financing in business development of innovative technologies for SMEs, a method of estimating technology maturity has been highlighted during the conference. Technology readiness levels (TRL) is a method of estimating technology maturity of Critical Technology Elements (CTE) of a program during the acquisition process. TRL is based on a scale from 1 to 9 with 9 being the most mature technology. High tech start-up usually approach from level 3 (proof of concept) to reach level 7 (system prototype demonstration in an operational environment). The main problem is that to finance the research process divided into three phases, the entrepreneur must apply three times with a huge waste of time.

In conclusion, more flexibility is expected: EU funding system is structured in a too strictly way. SMEs need more flexibility in financial resources utilization - low barriers for changes in projects costs structure.

[The FFWD EUROPE](#) project focuses on the definition and implementation (or upgrade) in each of the project regions of public-supported business accelerators or accelerator programs, with



the aim to foster access to private equity and international development opportunities for SMEs with significant growth potential. The project hereby builds on the concept of business accelerators, which was first implemented in a growing number of private initiatives and is being increasingly also adopted in the framework of public or public-private support schemes to entrepreneurs.

High growth enterprises contribute by more jobs than enterprises with moderate growth rates. The central issue addressed by the FFWD EUROPE project is how to create and support such high growth enterprises, which is a concern of most regions across EU. The consortium development builds on the identification of EU regions sharing the same needs concerning the support of SMEs growth and access to external private or public funding.

Three common challenges have been identified by the partners: Duplication of accelerator models in Europe, Internationalisation of companies and Access to finance. Access to finance, especially private funding, is a major challenge for companies with high growth potential. One of the goal of FFWD EUROPE is to show how the accelerator model provides opportunities to answer this challenge to some extent.

[ATM for SME](#) (Access to Microfinance for Small and Medium-sized Enterprises) see micro-finance as an outstanding solution to SME's and social entrepreneurship which can't access to traditional credit. **There is a wide variety of microfinance programs across Europe. However, there are significant differences in how these microfinance initiatives reach their target groups.** The project goal is to improve the access to micro-finance in participating regions by sharing and exchanging the local knowledge on innovative solutions. Many good practices have been identified. We have selected a few of these in different countries.

In Hungary, the municipality of Székesfehérvár by the initiative of Fejér Enterprise Agency (FEA) approved the "Interest Subsidy Scheme based micro enterprises" tailored for the smallest local enterprises. The funding of the credit scheme is guaranteed by FEA. Moreover the Municipality is subsidizing the average 6% interest on microcredit schemes so that it can be reduced to 2.5%. At national level, the combined scheme of the Hungarian Ministry of economy offer a grant and a loan at 2% interest rate. The requested loan amount must always be larger than the grant. The required minimum own resources from SMEs is 10%. Projects may include actions for improving energy efficiency.

In Spain, various micro-credits exist. The amount and the interest rate are different from a region to another. But generally loans are provided without guaranty and they are associated with advice and training. In some region this support concerns only disadvantage public (young people, women, migrants...).

In Germany, DMI gathers the Micro Finance Institutions (MFI). It developed an online platform which includes a risk warning system to ensure their sustainability: MFIs have to cover 20% of the first loss of their portfolio from their own resources. In this country the bank scoring model to evaluate risk of loans is not relevant to small innovative business. That's the reason why a trust-based partnership model has been launched by the banking system and the MFI institutions. Different initiatives are taken under this initiative. We could mention for example the evaluation of the entrepreneurial skills of the entrepreneur in order to deliver a loan but also a sharing risk mechanism which allows different stakeholder to invest and participate (a leverage of 5x can be realised thanks to this mechanism).

In Sardinia (Italy), many good practices have also been identified. To facilitate the access to credits for disadvantaged persons or at risk of financial exclusion, the "fund act" is a guarantee at the request of the credit organism. In order to boost social entrepreneurship and to increase



the capitalization level, a “risk capital investment for cooperatives” has also been created by the Sardinia region. At last, IMPRINTING is a micro credit instrument which consist to deliver loans at free interest rate and easy credit conditions in favour of disadvantaged subjects (women, NEET, migrants...): this loan can be delivered before the business creation when the project initiator is writing his business plan.

The Croatian Bank for Reconstruction and Development (HBOR) offers microcredit to micro enterprises for self-employment. HAMAG BICRO is an initiative of the national agency for SME’s investment which consist to analyse the financial and economic document of the SME’s project and to ascertain if a guarantee can be given (the guarantee can be from 30 to 80% of the loan).

In Poland, the National Association for Entrepreneurship Support (NAES) support long term unemployed people. The programme combine training on entrepreneurial skills and a grant up to 85% of the amount needed to launch a new business.

More detailed on these good practices and also others is available on the website on the [library](#) section.

4. In conclusion

Experiments have been carried out in many Regions in the field of the access to finance for innovative SMEs and especially in the early stages of their business. On this issue, most of the projects identified contribute mainly to the sharing of experiences in order to highlight good methods facilitating the access to finance for SMEs and to support their transnational transfer towards more regions.

We can note that a few Regions involved in EU projects have develop a Policy Implementation Plan based on exchange of experience on good practice to improve own policies tackling access to finance for SMEs, innovation, internationalisation and sustainable growth.

Moreover, thanks to the exchange of best practices in the frame of EU projects, Regions can mainstream actions proved by other Regions into their policies.

The sharing of the best practices resulting from the projects also shows mainly the need to effectively support these SMEs, as it is evidenced by the greater success of those that are supported by incubators or who benefit from mentoring programs. It’s a proven fact that this mode of support make the access to finance easier.

Image credit: Photo by Pixabay from [Pexels](#)

#Competitiveness #growth #start-up #financing #SMEs #PolicyLearning
#InterregEurope #EuropeanPolicy #COSME



Interreg Europe Policy Learning Platform on SME competitiveness

Thematic manager: Philippe Delearde
p.delearde@policylearning.eu

Thematic expert: Jean-Charles Minier
jc.minier@policylearning.eu

www.interregeurope.eu

July 2017